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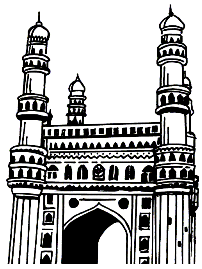

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1.1 Life Insurance

Q1. Define Life insurance.

(OR)

What is meant by life insurance.

Ans :

Meaning

The life insurance contract provide elements of protection and investment after getting insurance, the policyholder feels a sense of protection because he shall be paid a definite sum at the death or maturity. Since a definite sum must be paid, the element of investment is also present. In other words, life insurance provides against pre-mature death and a fixed sum at the maturity of policy. At present, life insurance enjoys maximum scope because each and every person requires the insurance.

Life insurance is a contract under which one person, in consideration of a premium paid either in lump sum or by monthly, quarterly, half yearly or yearly installments, undertakes to pay to the person (for whose benefits the insurance is made), a certain sum of money either on the death of the insured person or on the expiry of a specified period of time.

Definitions

(i) **According to J.H Maggee,** life insurance can be defined as "the life insurance contracts embodies an agreement in wkich the insurer undertakes to pay a stipulated sum upon the death of the insured or at designated time to a designated beneficiary.

(ii) **According to the section 2** of Indian insurance Act, 1938 "Life Insurance business is the business effecting contracts upon human life".

(iii) In simple words, life insurance can be defined as "the contract under which insurance company (insurer) agrees to pay certain amount incase of death or at the time of maturity of policy in consideration of periodical premium from the policy holder". It is usually considered as the better or smart way of investment for the benefit of protection against risk of death.

Q2. Explain the Evolution of life insurance.

Ans :

Life Insurance Policies and Life Insurance Plans have been around in India for as long as they have been around anywhere else in the world. In 1956, when the government nationalized the insurance sector by combining about 250 Indian life insurance companies to form a single firm, the Life Insurance Corporation (LIC) of India became the sole provider. This nationalization by the centre to channel more resources towards various national development programmes and give insurance market penetration a boost to protect the interests of the policy holders from failures which were the result of mismanagement resulted in the transformation of competitive segment to highly regulated monopoly. The nationalization also led to more effective mobilization of funds to enable capital to be allocated to various development projects.

In 1991, the Government implemented the New Industrial Policy, under which the Indian economy was opened up to foreign investment and sectors such as banking and finance were reformed. With the passage of the IRDA Act the Indian Life insurance industry was liberalized in 2000 with the objective of once again increasing competition in the industry and to tap the vast potential that this rapid growing market has to offer.

First year premium for single as well as regular life insurance policies offered by LIC and private players witnessed dynamic growth during the early 2000s — from less than 200 billion INR in 2002 to nearly 900 billion by 2009.

This intense competition has also forced the different life insurance players to improve their underwriting and risk management abilities. This has greatly benefitted policyholders and Life insurance companies have been quick to recognize the larger need for structured retirement plans, and the potential of long-term fund management.

Several unit linked insurance plans (ULIPs) have been introduced by private players and this has helped them to compete with LIC and also create a customer base of individuals who are willing to opt for these plans for purely investment & tax saving purposes. More than half of the premium income of private companies in the life insurance segment is contributed by these unit-linked plans. Traditional policies like term products and endowment based products form a relatively small proportion of the insurance market.

With the growing popularity of term insurance in India, spending on insurance is on a growth trajectory in India. However, the relatively high population growth rate has been slowing down the improvement of insurance density in India.

In 2006, a milestone occurred when India's insurance penetration nearly doubled to 4.10% before marginally declining to 4.00% in 2007. However, when compared to other countries, the life insurance market in India is still.

Q3. Explain the growth of insurance business in India.

Ans :

The term insurance was first conceptualized in the 14th century. It was used mainly for protection of sea travellers for conducting foreign trade. The concept of insurance has undergone a lot of changes since then. Due to the break up of traditional extended family system, insurance business got the opportunity to grow more.

The insurance business grew over a period of time with the advancement made in industry, trade and commerce. Currently, India stands in fifth position in terms of premium collection. The ratio of insurance premium to GDP is low despite of a two digit growth. Presently, out of more than one billion population, only 70 millions people are insured in India. The non-life insurance business needs to play an important role in protecting the properties of people. In 2000, the gross domestic premium income of general insurance business registered an increase of ` 9522 crores as compare to ` 184 crore in 1973.

Until 1956, 229 Indian insurance companies, provident insurance societies and 16 non-life Indian companies were conducting life insurance business in India. However, on 19th January, 1956, the government of India undertook the control and ownership of life insurance business. Since 1986, Life Insurance Corporation of India (LIC) was established with a bill passed in parliament. It was started functioning since 1st September 1956, Life Insurance business's growth is analyzed under new business which consists of group insurance business, new business individual insurances and not considering annuities, growth in assured sum and number of policies, average amount per policy, new rural business, business in force, number of offices, asset's productivity and process of new plans of insurance.

The insurance industry's performance is reflected by the overall performance of the economy. The underwritten of life insurance premium in India and abroad registered an increase of 24.31 in 2004-05 as compared to previous year. On other hand, non-life insurers registered a growth of 12.09%. The joint growth from both companies were 12.09% after adjusting for inflation. First year premium, single premium and renewal premium contributed 19.16%, 12.47% and 68.36% respectively.

In order to meet the need of insurance products for rural and urban poor, IRDA finalized and issued guidelines on micro-insurance. The regulations on micro-insurance gives a platform and rules to get insurance for selected segment.

As many insurance companies giving importance to unit linked business and to protect the interest of policy holders, the authority is finalizing the guidelines for this section.

The authority has acknowledged the importance for the growth of insurance in India. Due to the lack of regulations in health sector and prevailing malpractices in the system, the authority established a separate health insurance unit in IRDA on recommendations of health insurance working group.

Q4. What are the principles of Life Insurance?

Ans :

The various principles of life Insurance are as follows,

1. Principle of Insurable Interest

Principle of insurable interest is one of the legal principle of insurance contracts that supports the principle of indemnity. An insured should satisfy the requirement of insurable interest while collecting the amount by proving the loss due to misused peril. For example, A person has insurable interest in his car because he may lose financially if the car is stolen or damaged.

2. Principle of Indemnity

The principle of indemnity states that the insurer should not pay more than the actual amount of loss. In other words, it states that the insured should not make profits from the loss incurred by him. Several property and casualty insurance contracts are the contracts of indemnity.

3. Principle of Subrogation

Principle of subrogation is one of the legal principles of insurance contract and supports the principle of indemnity. This principle provides the benefit to insured to claim the insurer for any loss incurred due to the negligence of third party. Then, the insurer the can proceed against the third party to recover the loss paid to the insured.

4. Principle of Contribution

Principle of contribution refers to the insurer's right who has paid compensation for the loss under a policy, to recover a specific amount from the other insurers who are supposed to cover the loss. The principle of contribution supports the principle of indemnity.

5. Principle of Utmost Good Faith

Insurance contracts involve information asymmetries between parties. Generally, the insured has a better idea about the risk to be insured than the insurer. In order to balance this, the law specifies that both the parties should disclose any information important to the contract. The principle of utmost good faith specifies that both the parties should openly and honestly disclose the information without concealing any material facts that may affect the judgement of the other party.

6. Principle of Proximate Cause

Proximate cause is a legal term that describes how exactly the loss occurred. One should establish the cause of a loss as only risks particularly against can be compensated. The dominant and effective cause will be taken into consideration if there exists more than one cause for a loss. Thus, remote cause will not be considered here.

7. Principle of Loss Minimization

The principle of loss minimization states that the insured should not be irresponsible i.e., he must be careful and should take all the necessary steps to reduce the losses. He should not be careless after getting insured through a insurance contract. Thus, it is the responsibility of an insured to take safety measures. For example, wearing seat belts in a car to protect himself from an accident or fixing a CCTV camera to protect his valuables so that thefts does not occur.

Q5. What are the types of Life Insurance Plans?

Ans :

The Researcher, found the different types of Life Insurance Plans in the market. As we know that Life Insurance is important for everyone to protect family incase of their demise the insured money will save their family for educating their children and marriage etc. According to your needs, one can choose Life Insurance Scheme of any form.

1. Term Insurance Policy

This policy is pure risk cover with the insured amount will be paid only if the policy holder dies in the period of policy time. The intention of this policy is to protect the policy holder's family incase of death. For example, a person who takes term policy of Rs.500000 for 20 years, if he dies before 20 years then his family will get the insured amount. If he survive after 20 years then he will not get any amount from the insurance company. It is the reason why term policies are very low cost. So, this type of policy is not suitable for savings or investment.

2. Whole Life Policy

As the name itself says, the policy holder has to pay the premium for whole life till his death. This policy doesn't address any other needs of the policy holder. Because of these reasons this kind of policy is not very popular or insurance company not suggesting to take this policy.

3. Endowment Policy

It is the most popular Life Insurance Plans among other types of policies. This policy combines risk cover with the savings and investment. If the policy holder dies during the policy time, he will get the assured amount. Even if he survives he will receive the assured amount. The advantage of this policy is if the policy holder survives after the completion of policy tenure, he receives assured amount plus additional benefits like Bonus, etc. In this kind of policy, policy holder receives huge amount while completing the tenure. In addition to the basic policy, insurers offer various benefits such as double endowment and marriage/ education endowment plans. The cost of such a policy is slightly higher but worth its value.

4. Money Back Policy

Money Back Policy is to provide money on the occasions when the policy holder needs for his personal life. The occasions may be marriage, education, etc. Money will be paid back to the policy holder with the specified duration. If the policy holder dies before the policy term, the sum assured will be given to his family. A portion of the sum assured is payable at regular intervals. On survival the remainder of the sum assured is payable.

5. Annuities and Pension

An annuity is a series of periodic payments. An annuity contract is an insurance policy, under which the annuity provider (insurer) agrees to pay the purchaser of annuity (annuitant) a series of regular periodical payments for a fixed period or during someone's life time.

In an annuity, the insurer agrees to pay the insured a stipulated sum of money periodically. The purpose of an annuity is to protect against risk as well as provide money in the form of pension at regular intervals. Over the years, insurers have added various features to basic insurance policies in order to address specific needs of a cross section of people.

6. ULIPs

Unit linked insurance plan (ULIP) is life insurance solution that provides for the benefits of risk protection and flexibility in investment. The investment is denoted as units and is represented by the value that it has attained called as Net Asset Value (NAV). The policy value at any time varies according to the value of the underlying assets at the time.

In a ULIP, the invested amount of the premiums after deducting for all the charges and premium for risk cover under all policies in a particular fund as chosen by the policy holders are pooled together to form a Unit fund. A Unit is the component of the Fund in a Unit Linked Insurance Policy.

7. Joint Life Insurance

Two or more lives can be covered under one policy. Such policies usually cover married couples or partners. The SA is paid on the death of any of the insured persons during the term or at the end of the term. Some plans also provide payment of S.A. on the death of one life and the policy is continued to cover the second life till maturity without payment of further premium.

In the case of joint life insurances:

- A joint life declaration is necessary to create a joint interest in the policy.
- In case of partnership insurance, the partnership deed will be examined to ascertain the nature of financial interest of each partner.
- Each life will be underwritten separately.
- Bonuses accrue on the single basic SA only.

8. Childrens Plans

In these plans, risk on the life of the insured child will begin only when the child attains a specified age. Practices vary widely. The time gap between the date of commencement of the policy and the commencement of risk is called the 'Deferment Period'. If the child is 6 years old when the policy is taken and insurance is to begin when the child is 15 years old, the deferment period is 9 years. The date on which the risk will commence, at the end of the deferment period, is called the 'Deferred Date'. The deferred date will be a policy anniversary. Ages are reckoned as next birthday, nearest birthday or last birthday, as per the practice of the insurer.

There is no insurance cover during the deferment period. If the child dies during the deferment period, the premiums will be returned. Risk will commence automatically on the deferred date, without any medical examination. The main advantage of these plans is that the premium would be relatively low (age of the child at commencement) and cover will be obtained irrespective of the state of health of the child.

1.2 Premium

1.2.1 Meaning

Q6. Define premium. Explain different types of premium.

(OR)

Explain the concept of premium. What are the different types of premium.

Ans : **(Imp.)**

Meaning

Premium is an amount paid periodically to the insurer by the insured for covering his risk.

In an insurance contract, the risk is transferred from the insured to the insurer. For taking this risk, the insurer charges an amount called the premium. The premium is a function of a number of variables like age, type of employment, medical conditions, etc. The actuaries are entrusted with the responsibility of ascertaining the correct premium of an insured. The premium paying frequency can be different. It can be paid in monthly, quarterly, semiannually, annually or in a single premium.

Life Insurance Premium

Life insurance premium is the recurring or one-time payment you make towards your life insurance policy. A life insurance policy is valid only if your pay the premiums on time and according to the insurer's guidelines. In general, you have the option to choose the frequency of premium payments such as monthly, quarterly, half-yearly, yearly, or single premium. A factor of this premium is paid out as sum assured when the benefits of the policy get activated.

The premium for life insurance policies varies according to chosen plans as well as the credentials of the applicant. Usually, a younger, healthier individual will likely be quoted lower premium than a person touching his/her 50s. Similarly, a non-smoker will get preferential premium rates whereas a smoker is likely to be quoted a higher amount.

Types

There are various types of premium in Life Insurance :

1. **Risk Premium**

   As the name suggests, risk premium refers to the part of the payment that covers the underlying risk borne by the insurer. In case of life insurance, this would be the mortality risk (or the risk of death of the insured).

2. **Net (or) Pure Premium**

   It is the premium calculated after taking into account the interest likely to be earned by the insurer.

3. **Premium Loadings**

   Loadings are the incremental increases over the net or pure premium that an insurer does to cover for expenses like sales/sourcing or policy administration. It could also be loaded on account of bonus payouts that the insurer expects to make.

4. **Level Premium**

   Since the actual risk of the insured person varies with each passing year, the annual premium if re-calculated every year would result in an increasing outflow as premium payments. To counter this, Insurance companies sell policies with level premiums (premium payout stays constant through out the term)

5. **Single Premium**

   If the policy is purchased by someone who is not sure of his future ability to pay the premiums, the customer can opt for a single-premium payment option. Herein the payment is paid only once throughout the life cycle of the plan.

Q7. What are the factors considered in Calculating Premium ?

Ans : **(Imp.)**

A great way to help and protect your loved ones, is with Life Insurance which can be a huge investment as well. A lower premium paid can yield to a good amount of savings over a period of few years. Life insurance premiums are based on a number of factors, and it can be quite tedious for a few people to understand why and what the charges are, and why they pay a rate that may not be the same as another. There are some factors that many insurance companies consider when pricing their policies, there factor may not be within your control. But the life choices you make, can also lead to the factors that can affect your Life Insurance premium.

The factors that affect your premium towards Life Insurance are:

1. **Age**

   This is an obvious and not surprising factor that affects your Life Insurance premium, the age of the policyholder. If you're young the rates will be lower in comparison to someone older. The possibility of a young individual contracting a life threatening disease or to pass away in their youth is very unlikely. The insurance companies believe that you'll make many premium payments before they have to write a cheque for your family.

2. Gender

Insurance companies aren't against gender equality, but they believe there is a different life expectancy for different genders. As per the studies and statistical findings, women are believed to live 5 years more than men at the minimum. Therefore affecting the premium they pay, making them pay the premium for a larger period of time but at lower rate which is a plus point for the women.

3. Smoking

Smoking puts the policyholders at higher risk of all ailments, so if you're a smoker that that's as good as raising a red flag to the insurance companies. Most smokers pay a premium twice as much as non - smoker does, thus affecting the premium to a huge extent.

4. Medical history

There's isn't much one can do with the gene pool they come from. If a policyholder has a medical history of serious illnesses like cancer, heart diseases, or any other, then that makes them susceptible to get these from a hereditary perspective. Which increases the individual's premium by a larger margin than if their gene pool wasn't.

5. Health records

You as the policyholder will also need to provide your own health records. These records will ensure that you don't have any chronic diseases or potential health issues and keep your premium also in check instead of making a difference to it.

6. Drinking

Drinking of alcohol is injurious to health in more ways than one. If you as the policyholder are a heavy consumer of alcohol this can affect your premium at higher insurance rates. Insurance companies ensure to ask the applicant if they are smokers or drinkers.

7. The Policy

The policy itself also affects the premium you pay, the longer the tenure of the policy the larger the amount of the benefit at the time of death, since you're paying it for that period of time. Short term policies are more expensive that long term.

8. Profession

Profession also plays an important role in the premium you end up paying, any policyholder working in the mining industry, oil and gas, fisheries or any other dangerous profession increases the premium amounts you pay for the policy you decide to take.

9. Lifestyles Choices

Many insurers have a higher premium for people who love to takes risks for the thrill of it. Like speeding cars, climbing treacherous mountains or other high risk activities. Thereby increasing your premium to substantially more than other.

10. Obesity

Obesity is another factor that affects your premium as a policyholder, being obese can lead to a number of health problems like Osteoarthritis, High Blood Pressure, Cancer, Stroke, Coronary Heart Disease, causing overall health problems in the future and also increases your rates.

1.2.2 Premium Calculation

Q8. Discuss the calculation of premium for different types of policies.

Ans : **(Imp.)**

1. Term Insurance

Term insurance is also called as temporary insurance. It is one of the simplest contract where, thepayment is made only when the death of the life assured occurs within the specified term.

The following points are included in the calculation of term insurance. They are,

(a) The payment of premium is done only once in a single sum at the beginning of the policy.

(b) If life insured survives, the premium received in advance will not be returned.

(c) In case if the life insured does not die during the designated term, no amount will be paid to him.

(d) Death claims will be paid at the end of the year in which they occur but not at the end of the term.

(e) The term may be 1, 2, 5 or 7 years.

(f) As death may occur at any time and the insurance company is required to make payment, the insurer will calculate the probability of death in each year and the present value of the claim for each year.

The calculation of net single premium for each year will be as follows,

Present Value of Claims,

= No. of Deaths × Amount of Claims × Present Value of ` 1.

The formula for calculation of Net Single Premium is,

$$\text{Net Single Premium (NSP)} = \frac{Vd_s + V^2d_{x+1} + ... + V^2d_{x+n}}{l_x}$$

Where,

V denotes value of ` 1

d_x = Number of Deaths

l_x = No. of Living in the beginning

2. Net Single Premium in Whole Life Policies

A whole life policy is a policy which continues for the whole life of the policy holder and assures the payment to the beneficence upon the death of the insured. This policy is similar to the term insurance policy, but the only difference is that the term insurance is limited to a definite number of years, whereas the whole life policy continues for life time and will make the payment certainly at some time. Thus, if a person has taken policy at age 45, then the calculation will be continued upto 100th year. Therefore, premium calculation starts from the date of commencement of risk to the 100th year. The Net Single Premium in a whole life policy is calculated as follows,

Net Single Premium (NSP),

$$\frac{Vd_x + V^2d_{x+2} + V^3d_{x+3} \text{ ... for the end of the mortality table}}{l_x}$$

3. Net Single Premium in Pure Endowment Policy

Pure endowment policy is a policy where insurer assures to pay the amount to the policyholder, if he/she survives a certain fixed period. It is not possible for the insured to obtain the invested money in a pure endowment before the completion of endowment period. During this period, if the insurer dies, all the premium paid is forfeited. Therefore, the policyholder of 10 years pure endowment will be paid only when he survives till the completion of 5 years.

4. Net Single Premium in Ordinary Endowment Policy

In ordinary endowment policy, the amount of claim is paid at the survival of the term or at the death of the policyholder whichever is earlier. In this case, there is an assurance of payment. As the payment is made on the basis of death and survival, the net premium is calculated on the death rate and survival rate. The formula for calculating net single premium in ordinary endowment is as follow,

$$\text{Net Single Premium (NSP)} = \frac{Vd_x + V^2 d_{x+1} \ldots\ldots V^n d_{x+n-1}}{l_x} + \frac{V^n\, l_{x+n}}{l_x}$$

5. Net Single Premium in Double Endowment

In double endowment policy, if the life insured survives till the end of the term of policy, double of the amount is paid to him. If the death occurs within the term, then only single amount is paid. Therefore; this policy is similar to ordinary endowment policy only with a difference that if life insured survives upto the term, then double of the policy amount is to be paid. As the amount paid at the survival is double of the policy, another premium is also added based on pure endowment to the premium of ordinary endowment policy. The formula of Net Single Premium in double endowment is,

$$\text{Net Single Premium (NSP)} = \frac{Vd_x + V^2 d_{x+1} + V^2 d_{x+2} \ldots\ldots V^n d_{x+n-1} + 2V^2\, l_{x+n}}{l_x}$$

6. Net Single Premium for a Joint Life Policy

A joint life policy is a policy where the claim amount is paid at the first death of the assured lives who could be two or more. In this policy, the calculation process will be same as the term insurance except that the probability of death is compound one. The calculation of compound probability is done by addition of the probability of deaths of one another and with all of the old aged. The formula for calculating the compound probability is,

$$\text{Compound Probability} = 1 - \left[\frac{\text{Probability of Survival}}{\text{Younger Life}}\right] \times \left[\frac{\text{Probability of Survival}}{\text{Older Life}}\right]$$

7. Net Single Premium for Last Survival Policy

In this policy, the policy amount is paid only when all lives covered by the policy are expired. All the policy holder's compound probability is calculated which will continue till the youngest life's reaching to the highest age of the mortality table. This series will not end at first death. Therefore, the compound probability is calculated as,

Compound Probability = Probability of Death of One Person × Probability of Death of Other Person.

The calculation ends when the youngest one is supposed to be dead.

1.2.3 Rebates

1.2.3.1 Mode of Rebates

Q9. Define Rebate. State the various modes of Rebates.

Ans :

Meaning

Rebate is the amount paid for reduction, return or refund on what has been already contributed or paid. In a insurance policy, rebates can be of different types like, yearly, half-yearly, quarterly and monthly. Rebates are usually differ from plan to plan. It is very important to deduct permissible rebate for mode of payment of premium and sum assured for insurance.

Mode of Rebates

There are four types of modes of rebates which are used in the calculation of insurance premium. They are as follows,

1. Yearly mode of rebates
2. Half yearly mode of rebate
3. Quarterly mode of rebate
4. Monthly mode of rebate.

When the premium are paid on yearly or half-yearly basis, then there will be saving of administrative expenses compared to quarterly mode of rebate. In yearly and half-yearly modes, the insurer issues less number of notices, collection receipts and consequential entries. Thus, administrative cost get reduced. However, in monthly mode, the extra premium is to be charged by insurer to cover additional administrative expenses.

This is summarised below,

(i) When less number of premium installment are there, then higher will be the amount and more will be the f& discount.

(ii) When more number of premium installment are there, then less will be the amount and discount.

Premium

$$= \text{Sum Assured} \times \frac{\text{Rate of Premium}}{1000}$$

However the mode of rebate (Payments) for yearly, half-yearly, quarterly and monthly are listed below,

1. Yearly - 3% less than the table rate
2. Half-yearly - 1.5% less than the table rate
3. Quarterly - Nil
4. Monthly - 5% more than the table rate (it is to be added).

1.2.3.2 Large Sum Assured Rebates

Q10. Define Large Sum Assured Rebate. State its mode.

Ans :

Large sum assured rebates are made for high sum assured or amount. However, every insurance company follow different rates but the oldest and popular insurance company, Life Insurance Corporation (LIC) follows the following discount structure,

(a) ` 25,000 - ` 49,999, ` 1 less than tabular premium.

(b) ` 50,000 and above, ` 2 less than tabular premium.

Mode

For Regular Premium Policies	
Sum Assured	**Rebates**
50,000 to 1,00,000	Nil
1,05,000 to 3,00,000	1% S.A
3,05,000 and above	2% S.A

For Single Premium Policies	
Sum Assured	**Rebates**
50,000 to 1,00,000	Nil
1,05,000 to 3,00,000	5% S.A
3,05,000 and above	10% S.A

PROBLEMS

1. **From the given information, calculate premium for yearly payment.**

    Sum assured: ` 60,000

    Term: 30 years

    Age: 25 years

    Tabular premium/1000 (Quarterly mode) ` 40

    Rebate for large sum assured: ` 2 per 1000

    Rebate for yearly payment: 2%

Sol :

Calculation of Premium for Yearly Payment

Particulars	**Amount (`)**
Tabular Premium (Quarterly mode / 1000)	40.00
Less: Rebate for large sum assured	2.00
	38.00
Less: Rebate for yearly payment $\left[40 \times \frac{2}{100}\right]$	0.8
	37.2
Premium = $37.2 \times \frac{60,000}{1000}$	2,232

$\therefore$ Premium for yearly payment = ` 2,232

2. **From the given information, calculate premium for Half - Yearly payment,**

    Sum assured: ` 60,000

    Term: 30 years,

    Age: 25 years

    Tabular premium / 1000 (Quarterly mode) ` 40

    Rebate for large sum assured: ` 2 per 1000

    Rebate for half - yearly payment.

Sol :

Calculation of Premium for Half Yearly Payment

Particulars	Amount (`)
Tabular Premium (Quarterly mode / 1000)	40.00
Less: Rebates for large sum assured	2.00
	38.00
Less: Rebate for Half yearly payment $\left[30 \times \frac{1.5}{100}\right]$	0.60
	37.40
Premium (Half yearly) $= 37.40 \times \frac{60,000}{1000}$	2,244
Premium (Half yearly installment) $= \frac{2,244}{2}$	1,122

$\therefore$ Premium for half yearly payment = ` 1,122

3. From the given information, calculate premium for monthly payment.

Sum assured: ` 60,000

Term: 30 years

Age: 25 years

Tabular premium/1000 (Quarterly mode) ` 40

Rebate for large sum assured: ` 2 per 1000

Add for monthly payment: 10%

Sol :

Calculation of Premium for Montly Payment

Particulars	Amount (`)
Tabular Premium (Quarterly mode / 1000)	40.00
Less: Rebates for large sum assured	2.00
	38.00
Less: Monthly mode $\left[40 \times \frac{10}{100}\right]$	4.00
	42.00
Premium (Yearly) $= 42 \times \frac{60,000}{1000}$	2,520
Premium (Monthly) $= \frac{2,520}{12}$	210

$\therefore$ Premium for half yearly payment = ` 210

1.2.4 Premium Loading

Q11. What is loading and premium loading?

Ans :

(i) Loading

Loading is the costs of an insurance policy. It is a type of cost which includes selling and administrative costs like, marketing cost, employees salaries, cost associated with brokers, agents and premium taxes. Cost of capital is also one of the component of loading which is more difficult to understand.

The cost of capital is a kind of reserves which enable the insurance company (insurer) to pay unexpected by higher claims. In this case, loading include a amount which covers the transactions costs associated with making these assets available to insurance company. Addition to this, it also include higher tax cost to the investor associated with such investment. The loading is usually expressed in percentages of premium, which is referred as premium loading factor.

(ii) Premium Loading

The premium loading refers to the margin which is require by a insurance company (Insurer) for covering up the overhead expenses and generating appropriate profit. It is calculated by using following formula,

Premium Loading Factor

$$= 1 - \frac{\text{Expected loss}}{\text{Premium}}$$

1.2.5 Rider Premiums - Computation of Benefits

Q12. What do you mean by rider benefits and rider premium? What are the benefits of riders?

Ans :

(i) Rider Benefits

An optional benefit available to the policy holder at an additional cost is known as rider benefit. In the pre-liberalisation period, the benefits under the products are predefined and offered as packages. Based on that, customers has to choose the plan according to his requirements. However, now a days the basic trend is the basic plan which is offered with add on benefits to match with the exact needs of the customer. The add on benefits with additional costs are defined as riders benefits.

(ii) Rider Premium

The extra premium paid to receive extra benefit from insurance policy is known as rider premium. Extra premiums are usually paid to compensate the extra risk or to secure extra disability or death benefits. The rider premium will be added after the calculation of actual premium. It is the last factor which is to be added in premium amount for availing extra benefits.

Benefits

Following points highlights the benefits of riders,

1. It increases the value of the insurance policy.
2. It can be availed only if the insurance premium for the basic benefits is being paid.
3. It will be stopped when basic premium of sum assured get stopped.
4. In some cases, it can be availed upto certain age of the insured.
5. It can be added to the insurance policy from the Date of Commencement (DOC) of the policy.
6. It also can be added from the policy anniversary based on the Date of Application (DOA).
7. It is the extra benefit to the insured which come with small premium payments. Such a premium is paid as extra premium for availing extra benefits.

Q13. Explain the popular rider benefits and their computation.

Ans :

1. Accident Benefits

Accident benefit is the most popular rider benefit, where the accident benefit is payable if the insured death was caused directly and independently of all other causes or by an accidental injury and death occurred due to,

(i) War and riot related accidents

(ii) Self imposition injuries (suicide)

(iii) Accidents from criminal activities

(iv) Accident from aviation activities

This benefit is given only when the incident is not accident (likely) and may not extend beyond 65 or 70 years of age of the life assured.

2. Disability Benefit

Disability benefit is provided when the policy holder suffers from total and permanent disability due to an accident. It is issued in periodical payments with a lumpsum at the end of the term of basic plan or on earlier death.

The policy holder is eligible for this policy only if the disability raised before the policy anniversary on which the policy holders life assured is 65 or 70 years. Addition to this, the accident must be total and permanent i.e., there should not be a chance that life assured can earn or obtain any wages, compensation or profit.

The policy holder is declared as permanent disable person in the following situations,

(i) Loss of sight of both eyes,

(ii) Amputation of hands or above the wrist,

(iii) Amputation of both feet or above the ankles,

(iv) Amputation of one hand or above the wrist and one foot or above the ankle.

There is a limit to claim the policy when the accident arise as specified in the policy. The policy holder will get 10% of sum assured every year till maturity/death whichever is earlier.

3. Income Benefit

Income benefit is the rider benefit where in case of premature death of the policy holder it provides regular financial support to the life assured's family. It not only provides lumpsum on death, in addition it gives a percentage of 1% every month on the basic sum assured.

This rider is designed in benefit of young men and women or who have a young family to support. In accordance with this, a monthly income is paid to surviving spouse/children of life assurer until a certain period of 10, 15, 20 years from the date of policy insurance.

4. Critical Illness Benefit/Minor Surgical Assistance Rider

If the policy holder is affected with critical illness such as malignant cancer, coronary artery bypass surgery, heart attack, kidney failure, stroke and major organ transplant after the lien period mentioned in the policy. The diagnosis proof should be as per the specified standards of the company. The bills of hospitalization treatment or purchase of medicine will not be claimed by them.

In equivalent to this, financial assistance is provided in case of major or minor surgery after attaining discharge report. However, no bills are required while claiming the policy. These riders are different from the earlier mediclaim policies provided by general insurance companies and these riders are new to India.

5. Term Assurance Rider

Term assurance rider provides the additional protection to cover the risk at the cheapest premium. For Example, a temporary loan raised for business or family expenses where, the policy holder can acquire this benefit at a nominal cost for a limited period?

1.2.6 Surrender Value – Paid up Value

Q14. What is Surrender Value? Explain the various steps for the calculation of Surrender Value.

Ans :

The term surrender value refers to the amount of money which the insurer agrees to pay in case the life assured decides to surrender his policy before its maturity. It is said that the policyholder wishes to surrender his policy to the insurer and gives up his claim on it. Surrender of policy indicates termination of the contract of insurance.

The amount of surrender value is determined on the basis of actual premium paid and the number of years the policy has been in force. Surrender value increases with each payment of premium. Payment is to be made against the full and final discharge of insurer's liability under the contract.

Steps

The calculation of surrender value involves the following steps :

(a) Calculate duration elapsed under the policy. This duration will be equal to data of calculation of surrender value less date of commencement to be rounded off to the nearer half year. In other words, The elapsed duration is calculated by deducting date of commencement of policy (DOC) from the date of First Unpaid Premium (FUP) i.e., Paid-up Duration = Date of FUP - DOC

(b) Calculate the paid up value, inclusive of vested bonus under with profit plans.

(c) Ascertain from the tables the appropriate surrender value factor per Rs. too/- paid-up value, corresponding to plan, duration elapsed and original term.

(d) Surrender Value = Paid-up × Surrender value Factor / 100.

According to Life Insurance Corporation of India, a policy acquires surrender value only after payment of two or three years premium. Thus, the policy is required to have run for three years before it acquires surrender value. In this regard, some Insurance companies guarantee a minimum surrender value of 40 per cent of the total premium paid.

Q15. What are the various surrender charges?

Ans :

1. Initial Expenses

At the time of commencement of contract, some expenses may incur for undertaking the proposals, payment of commission to medical officers and agents, correspondence and issuing of policy. As the initial expenses are very high, the premium of first year is not able to meet all the expenses. After the continuation of the policy for many years, these expenses are retrieved. In addition to this, the initial expenses are equally distributed over the premium paying period.

2. Adverse Financial Selection

When there is a decline in business, the financial position of the insurer gets reduced by the surrendering of policies. This is because many policyholders try to rush for surrender values and the funds of the insurer will also be reduced to minimum. In these situations, it is not allowed for the policyholders to obtain the surrender values more than the realized values of funds invested. The insurer is supposed to clear some of their assets at reduced prices.

3. Cost of Surrender

A certain amount of expenses are incurred by insurer in undertaking the surrender of policies. At times, the cost of surrender is like other expenses spread over the premium paying period. The cost is not realized in the surrender (early) and the deduction from the reserve is allowed.

4. Unfavourable Mortality Selection

The individuals who are in completely poor health, do not surrender their policies. These individuals will not only borrow or beg money but also steal inorder to sustain the protection. The persons who surrender their policies expect longer life when compared to the ones who do not. Accordingly at every surrender, the actual or average mortality may increase more than the anticipated mortality. While the surrender value is allowed, the rising mortality should be adjusted.

Q16. Explain the concept of Paid-up Value.

Ans :

If a policyholder discontinues the payment of premium after atleast two years premiums have been paid and subsequent premium is not paid, the policy does not become void, but continues as a paid-up policy. According to Insurance Act, it is defined as the policy paid up for an amount bearing the same proportion to the amount of original sum assured which the number of premiums paid bears to the total number of premiums payable under the policy as a whole

i.e., Paid-up Value

$$= \frac{\text{No. of Premium Paid}}{\text{No. of Premium Payable}} \times \text{ Sum Assured}$$

The amount (claim) would be available to the life on maturity or on death whichever is earlier. In case of participating policy, it is assured that bonus or profits will be added to the paid-up value, but future gains or profits are not entitled to such policy.

Note : If this figure is less than the guaranteed surrender value, latter is payable.

1.3 General Insurance

Q17. Define General Insurance. What are the objectives and functions of General Insurance.

Ans :

Meaning

General insurance refers to the insurance contracts that do not come under the field of life insurance. The different forms of general insurance are fire, marine, motor, accident and other miscellaneous non-life insurance.

The tangible assets are susceptible to damages and a need to product the economic value of the assets is needed. For this purpose, general insurance products are bought as they provide protection against unforeseeable contingencies like damage and loss of the asset. Like life insurance, general insurance products come at a prime in the form of premium.

Objectives

The main objectives of GIC were superintending, controlling, and carrying on the business of general insurance.

1. To provide need-based and low-cost general insurance cover to the rural population.
2. To administer a crop insurance scheme for the benefits of farmers.
3. To develop and introduce covers with social security benefits.
4. To develop a marketing network throughout the country and to promote balanced regional development and make insurance available to the masses.

Functions

The functions of GIC as mentioned in the Act were as follows :

1. The carrying on of any part of general insurance business as deemed desirable,
2. Aiding, assisting and advising the companies in the matter of setting up of standard of conduct and sound practice in general insurance business and in rendering efficient customer service.
3. Advising the acquiring companies in the matter of controlling the expenses including the payment of commission and other expenses.
4. Advising the acquiring companies in the matter of investment of funds.
5. Issuing directions to acquiring companies in relation to the conduct of general insurance business.

Q18. What are the differences between Life Insurance and General Insurance?

(OR)

Compare and contract Life Insurance and General Insurance.

Ans :

S.No.	Basis for Comparison	Life Insurance	General Insurance
1.	**Meaning**	Life insurance can be understood as the insurance contract, in which the life risk of an individual is covered.	General insurance refers to the insurance, which are not covered under life insurance and includes various types of insurance, i.e. fire, marine, motor, etc.
2.	**Term of contract**	Long term	Short term
3.	**Claim payment**	Insurable amount is paid, either on the occurrence of the event, or on maturity.	Loss is reimbursed, or liability incurred will be repaid on the occurrence of uncertain event.
4.	**Premium**	Premium has to be paid over the years.	Premium should be paid in lump sum.
5.	**Insurable interest**	Must be present at the time of contract.	Must be present, both at the time of contract and at the time of loss.
6.	**Policy Value**	It can be done for any value based on the premium the policy holder willing to pay.	The amount payable under non-life insurance is confined to the actual loss suffered or liability uncured, irrespective of the policy amount.
7.	**Savings**	Life insurance place has a component in savings.	General insurance has no such savings component.

1.4 General Insurance Policy Documents and Forms

Q19. Explain the various General Insurance Policy Documents and Forms.

(OR)

What are the various documents of General Insurance?

Ans :

Documents are necessary to evidence the existence of a contract. In life insurance several documents are in vogue. The documents stand as a proof of the contract between the insurer and the insured. The major documents in vogue in life insurance are premium receipt, insurance policy, endorsements etc.

There are various insurance documents used for different types of insurance, which are essential for all classes of insurance business. The object of insurance documents is given to the insurer full particulars of the risk against which insurance protection is desired. It also provides evidence of contract into which the parties have entered.

1. Proposal Forms

The company's printed proposal form is normally used for making an application for the required insurance cover. The proposal form contains questions designed to elicit all material information about the particular risk proposed for insurance. The number and nature of questions vary according to the particular class of insurance covered.

In Marine Cargo Insurance, Insurance document is not the practice to use a proposal form, although sometimes it is usual to obtain a questionnaire or a declaration form duly completed. Proposal forms are used for hull insurance.

In Fire Insurance, the practice varies among the companies, proposal forms are not generally used for large industrial risks where inspection of the risk is arranged before acceptance of the risk. Forms are used for simple risks. Proposal forms are used in respect of risks which are normally declined but have to be accommodated to retain the goodwill of the client.

In Miscellaneous Insurance, proposal forms are invariably required and they incorporate a declaration which extends the common law duty of good faith. Fire proposal forms may or may not have the declarations. The following items may be considered as common to all proposal forms.

- Proposer's name in full
- Proposer's address
- Proposer's profession, occupation or business
- Previous and present insurance
- Loss experience
- Sum insured
- Other Section's - Signature, date, place etc.

2. Policy Forms

Policy forms, like proposal forms, vary within wide limits as between different classes of insurance but they have certain features in common. The policy is a document which provides evidence of the contact of insurance. This document has to be stamped in accordance with provisions of the Indian Stamp Act 1899. Where the insurance is governed by a Tariff or a Market agreement, the policy wording is prescribed therein itself and it is obligatory for insurers to use these wordings. In fire and miscellaneous insurance, the policy form used is on a scheduled basis i.e. all individual details relating to a particular insurance are grouped together in a schedule. Generally speaking policies are divisible into certain well defined sections and these are as follows:

- Recital Clause or Preamble
- Operative Clause
- Attestation Clause
- Conditions
- Schedule

3. Cover Note

A cover note is a document issued in advance of the policy. It is issued when the policy cannot for some reason or the other, be issued straight away. Cover notes are issued when the negotiations for insurance are in progress and it is necessary to provide cover on a provisional basis or when the premises are being inspected for determining the actual rate applicable. Pending the preparation of the policy, the cover note is issued as evidence of protection for a temporary period of time and to prove that cover is in force. Here is a brief detail of cover.

In Marine Insurance, marine cover notes are normally issued when details required for the issue of policy such as name of the steamer, number of packages or exact value etc. are not known. In Fire Insurance,, the operative clause of a fire cover note is issued in consideration of the proposer named in the schedule having proposed the effect of an insurance against fire for the period mentioned, on the usual terms and conditions of the company's policy. In Motor Vehicle Insurance, motor cover notes are to be issued in the form prescribed by the Motor Tariff.

4. Certificate of Insurance

In motor insurance, in addition to the policy, a certificate of insurance is required by the Motor Vehicle Act. 1988. This certificate provides evidence of insurance to the Police and Registration authorities. It contains the essential features of the cover including the terms and conditions. In Marine Insurance, certificate of insurance is issued to provide evidence of cover on shipments insured under cargo open cover or floating policies.

5. Endorsements

It is the practice of insurers to issue policies is a standard form, covering certain perils and excluding certain others. If it is intended, at the time of issuing the policy to modify the terms and conditions of the policy, it is done by setting out the alteration is a memorandum which is attached to the policy and forms part of it. The memorandum is called an endorsement.

1.5 General Insurance Products

Q20. Write about General Insurance Products.

(OR)

Explain the different types of General Insurance Products.

Ans : **(Imp.)**

General insurance is a contingent contract with the aim of providing security against the risk. It is a short term contract, the premium of which varies according to the renewal of the insurance contract. The following are the different types of general insurance products,

1. Fire Insurance

According to Indian Fire Insurance Act, 1938, "In addition to other insurances, fire insurance is that insurance contract which takes place against fire and such other risks which are mentioned in the fire insurance "contract".

2. Marine Insurance

According to Marine Insurance Act, 1963 "marine insurance is an agreement whereby the insurer undertakes to indemnify the assured, in the manner and the extent thereby agreed, against losses incidental to marine adventure".

3. Motor Insurance

Motor vehicle insurance was emerged in United Kingdom, but later on it has gained importance in the whole world. This type of insurance cover risk of owner and vehicle along with the financial liability which may develop from accident causing harm to third party. When there is no insurance all the expenses relating to repair of vehicle, treatment of injured must be borne by the person. Hence, motor vehicle insurance is essential. In India, motor vehicle insurance is made compulsory after the amendment of Act for motorists to insure against the risk of liability to third parties.

4. Liability Insurance

Liability insurance is a mandatory form of insurance for those at risk of being sued by third parties of negligence or other tortuous actions. The regular classes of mandatory policy gives coverage for the ones who provide professional services to the public, for the drivers of vehicles, for those who employ staff and for those who manufacture products which may cause harm.

5. Personal Accident and Speciality Insurance

Personal accident insurance aims at paying a fixed amount of compensation to person who met with an accident leading to death or disablement in body due to accidental injury.

During policy period, if policy holder gets injured solely and directly from accident then insurer pay then policy amount to insured or to his legal nominee in case of death, permanent disablement, partial disablement etc. Claim amount of policy will be paid only once in case of death. Some policies make payment for education of dependent children.

Speciality insurance refers to the insurance policy that is taken up for special and unique items, This insurance policy covers unique and important items, which are generally not covered under the general insurance policies. Some examples of speciality insurance items include the following,

(a) Pet animal health insurance.

(b) Insurance of vintage cars or furniture.

(c) Insurance of voice (in case of a professional singer).

6. Engineering Insurance

Engineering insurance is also known as machinery breakdown or plant all risks insurance. This policy provide wide coverage of damages caused to electrical and mechanical machinery. Even the losses suffered by contracts and principals relating to civil engineering projects such as bridges, tunnels, building, etc are covered under this policy.

7. Other Insurance

Miscellaneous or other general insurance comprises of different insurance coverages which are prepared to fulfill the unusual requirements of different individuals.

1.5.1 Fire Insurance

Q21. What is Fire Insurance ? Discuss, its features and scope.

Ans :

Fire insurance provides protection against damage to property caused by accidents due to fire, lightening or explosion, whereby the explosion is caused by boilers not being used for industrial purposes. Fire insurance also includes damage caused due to other perils like storm, tempest or flood, burst pipes, earthquake, aircraft, riot, civil commotion, malicious damage, explosion, etc.

Section 2 of the Insurance Act 1938 defines fire insurance as "The business of effecting, otherwise than incidentally to some other class of insurance business, contract of insurance against loss by or incidental to fire or other occurrence customarily included among the risks insured against in fire insurance policies".

Features

There are few salient features of fire insurance:

(i) **Written Contract :** It means that fire insurance do the contract between insured and insurer.

(ii) **Two Parties :** In fire insurance the contract is made between two parties, i.e., insured and insurer.

(iii) **Period of Insurance :** This type of insurance is done maximum for one year.

(iv) **Only Protection Element :** Here, in fire insurance, only protection element is present and lacks investment elements.

(v) **Use of Word Insurance :** In fire insurance 'insurance' word is used instead of 'assurance'. This means the compensation will be paid only if there is loss.

Products

The policies can be of various types which are explained below :

1. Valued Policy

The value of the property to be insured is determined at the inception of the policy. In this case, the insurer pays the total admitted value irrespective of the then market value of the properties.

2. Specific Policy

Where a specific sum is insured upon a specified property in case of a specified period, the whole of the actual loss is payable provided it does not exceed the insured amount. Here the value of property insured has no relevance in arriving at the measure of indemnity in a specified policy and the insured sum sets a limit up to which the loss can be made good.

3. Floating Policy

The floating policy is the policy taken to cover one or more kinds of goods at one time under one, sum assured for one premium and in relation to the same owner. This policy is useful to cover fluctuating stocks in different localities.

4. Average Policy

Policy containing ‘average clause’ is called an Average Policy. The amount of indemnity is determined with reference to the value of the property insured. If the policyholder has taken policy for lesser amount than the actual value of the property, the insured will be deemed to be his own insurer for the amount of under-insurance. The insurer will pay only such proportion of the actual loss as his insurance amount bears to the actual value of the property at the time of loss.

5. Declaration Policy

Under the declaration policy, the insured takes out insurance for the maximum amount that he considers would be at risk during the period of the policy. On a fixed date of every month or a specific period, the insured furnishes a declaration of the amount. The premium is provisionally paid to 75% of the annual premium amount.

6. Adjustable Policy

This policy is nothing but an ordinary policy on the stock of the businessman with liberty to the insured to vary at his opinion, the premium is adjustable pro rata according to the variation of the stock.

7. Reinstatement Policy

This policy is issued to avoid the conflict of indemnity. In other types of policies only the market value of the damage or loss is indemnified but this policy undertakes to reinstate the insured property lost by fire to new condition irrespective of its value at the time of loss.

8. Comprehensive Policy

This policy undertakes full protection not only against the risk of fire but combining within the risk against burglary, riot, civil commotion, theft, damage from pest, lightning. The policy is also termed as ‘All in policies’. Here the ‘Comprehensive’ does not mean that every type of risk is covered. There may be many exclusions and limitations. This policy is beneficial to the insured and the insurer. The insurer can get higher premium and the assured is protected against losses due to several specified perils.

9. Consequential Loss Policy

The fire insurance is originally purchased to indemnify the material loss only. The intangible interest was not indemnified. This provided a check on the insured to exercise a greater care with respect to the property. However, the settlement of a loss covering material damage only was not sufficient. The consequential loss was also to be provided. Thus, the consequential loss policy includes the loss of tangible and intangible properties.

Scope

Standard Fire and special perils policy usually cover loss due to the following perils:

1. Fire

Destruction or damage to the property insured by its own fermentation, natural heating or spontaneous combustion or drying process can not be treated as damage due to fire.

2. Lightning

It may result in fire damage or other type of damage, such as cracks in a building due to a lightning strike.

3. **Explosion**

An explosion is caused inside a vessel when the pressure within the vessel exceeds the atmospheric pressure acting externally on its surface. This policy, however, does not cover destruction or damage caused to the boilers or other vessels where heat is generated.

4. **Storm, cyclone, typhoon, hurricane, tornado, landslide**

These are all various types of violent natural disturbances accompanied by thunder or strong winds or heavy rain fall. Loss or damage directly caused by these disturbances are covered excluding those resulting from earthquake, volcanic eruption etc.

5. **Bush fire**

This covers damage caused by burning of bush and jungles but excluding destruction or damage caused by forest fire.

6. **Riot, strike, malicious, and terrorism damages**

Any loss or physical damage to the property insured directly caused by such activity or by the action of any lawful authorities in suppressing such disturbance is covered.

7. **Aircraft damage**

Loss, destruction or damage caused by Aircraft, other aerial or space devices and articles dropped there from excluding those caused by pressure waves.

8. **Overflowing of water tanks and pipes etc.**

Loss or damage to property by water or otherwise on account of bursting or accidental overflowing of water tanks, apparatus and pipes is covered.

Q22. Define Fire Insurance contract. What are the principles of fire insurance control?

Ans :

Fire insurance is a contract of indemnity in which the insurer is responsible is indemnify the insured against any financial loss or damage to the insured property due to fire caused directly anytime in an agreed period of time.

Insurable Properties Covered by Fire Insurance Contracts/Subject Matter of Fire Insurance

Insurance cover can be taken up for any movable or immovable property which have a pecuniary value can be insured against fire. As fire insurance contracts are governed by tariff the property which is being insured should be described accordingly. These include the following,

1. Electrical installation in buildings.
2. Contents of buildings such as machinery, plant and equipment, accessories etc.
3. Buildings.
4. Goods and stock.
5. Goods i.e., Raw materials, work in progress, semi-finished goods, finished goods, packaging materials in factories and godowns.
6. Furniture, fixture and fittings.
7. Pipelines situated inside or outside the compound etc.
8. Contents in dwellings, hotels, shops etc.

Principles of Fire Insurance Contract

The following principles are necessary for a valid fire insurance contract,

1. **Principle of Indemnity**

The aim of this principle is to put the insured in the same financial position to maximum extent possible after the loss had occurred. Only the price of actual loss subject to the sum assured can be recovered by the insured.

2. **Principle of Insurable Interest**

The insurable interest should be present at the time of the loss and also at the time of effecting the insurance. The insurable interest may arise in a contract of sale or purchase as it may be legal. The following are believed to have insurable interest in the subject-matter in the context of life insurance, Trustee, owner, mortgagor, executor, bailee, warehouseman, finder, tenants who are liable to pay rent after the fire etc. However the persons can insure upto an extent of limited interest.

3. Principle of Good Faith

Contracts of fire insurance are contracts of "uberrimae fidei" i.e., a contract based on unconditional good faith. As per this principle, the insured should furnish full and detailed information of all material facts possible to affect the fire officials judgement in deciding the premium rates whether the proposal need to be accepted or rejected.

4. Principle of Causa Proxima / Loss Through Fire

In a fire insurance contract, the loss resulting from fire or some other related cause being the proximate cause of loss are covered. If the fire is caused by the insured himself or with his assistance or by the operation of a peril specifically excluded under the policy such as earthquake, the loss will not be covered and the insurer will not be liable to indemnify the insured.

5. Principles of Subrogation and Contribution

Fire insurance contracts relies on the principle of subrogation while states the insurer becomes entitled to claim all the rights of the insured after paying compensation against third parties who may be responsible directly or indirectly for causing such a loss. Fire insurance contracts are also governed by the principle of contribution which state that where the subject matter has been insured by more than one insurer, every insurer has to meet the loss only rateably. If the insured has paid more than his share of loss he is entitled to recover the excess amount paid by him from his co-insurers.

6. Yearly Contract

A fire insurance policy is generally for one year and can be renewed from then.

Q23. State the Procedure of effecting Fire Insurance.

Ans :

For obtaining fire insurance policy, a property holder must follow the following procedure.

1. Selection of insurance
2. Proposal form
3. Evidence of respectively
4. Survey of the property
5. Acceptance of proposal
6. Issue of cover note
7. Issue of insurance policy / bond

1. Selection of insurance

First of all a policy holder must select the insurance company for fire insurance. The company having good financial position and ideal terms and condition against fire insurance and ideal terms and condition against fire insurance must be referred.

2. Proposal form

After selecting of the company, a proposer must fill up the proposal form, which can be obtained free of cost from insurance company. It contains different question regarding the value, nature, time, construction of the property to be insured and answer of various question must be filled by insured and answer of various question must be filled by the proposer. The proposal form also include name, address, occupation of proposer together with insured amount, types of policy, method of paying premium, etc. All the details regarding property should be cleared and true. False matter should not be included. After filling the information in proposal form, the proposer should sign it.

3. Evidence of respectively

It is a recommendation provided by an individual, institution, firm or a company about some person. In fire insurance there is much physical and moral hazards (risk). Physical hazards arise from the nature, design or site of insured property. And the moral hazard means the character of the proposer. Evidence of respectively is required for the fire insurance because sometimes a policy holder may destroy the property himself to claim on insurance company. In order to safe from these risks, insurance company collects evidence of honesty, integrity and financial position of the proposer from the third party. If the insured amount is not very high or proposer is well known in the society then evidence of respectively is not required.

4. **Survey of the property**

Generally insurance company issues the insurance policy on the basis of proposal from but sometimes the risk is high, the insurance company surveys the property and risk is determined. For survey of the property, insurance company can appoint the surveyor.

5. **Acceptance of proposal**

After submitting of necessary document in the insurance company office, the officer scrutinize the documents and if the documents are recording to demand then the form is accepted and letter of acceptance with the rate of premium is sent to the proposer and first insurance premium will also be demanded by insurance company.

6. **Issue of cover note**

When the proposer deposit the first premium then insurance company issue the cover note because the fire insurance process is very lengthy. Cover note is an interim protection note, work as an insurance policy and liability of the company will start from the date in which cover note is issued.

7. **Issue of insurance policy/bond**

At least insurance company will issue the insurance policy which is dully stamped and contains terms and conditions against fire insurance. It is legal and formal document of fire insurance.

1.5.2 Marine Insurance

Q24. What is marine insurance ? Explain the features of marine insurance in general insurance.

Ans :

Meaning

Marine insurance basically covers three risk areas, namely: hull, cargo and freight. The risks which these areas are exposed to are collectively known as "Perils of the Sea". These perils include theft, fire, collision, etc. Section 2(13)A of the Insurance Act 1938 defines marine insurance as, "Marine insurance business" means the business of effecting contracts of insurance upon vessels of any description, including cargoes, freights, and other interests which may be legally insured in or in relation to such vessels, cargoes and freights, goods, wares, merchandise and property of whatever description insured for any transit by land or water or both, and whether or not including warehouse risks or similar risks in addition or as incidental to such transit and includes any other risks customarily included among the risks insured against in marine insurance policies.

Features

The salient features of marine insurance are as follows :

1. It is based on utmost good faith. Both the insured and the insurer must disclose everything which is in their knowledge and can affect the contract of insurance.

2. It is a contract of indemnity. The insured is entitled to recover only the actual amount of loss from the insurer.

3. Insurable interest in the subject-matter insured must exist at the time of the loss. It need not exist when the insurance policy is taken. Under marine insurance, the following persons are deemed to have insurable interest :

   i) The owner of the ship.

   ii) The owner of the cargo.

   iii) A creditor who has advanced money on the security of the ship or cargo.

   iv) The mortgagor and mortgagee.

   v) The master and crew of the ship have insurable interest in respect of their wages.

   vi) In case of advance freight, the person advancing the freight has an insurable interest if such freight is not repayable in case of loss.

4. It is subject to the doctrine of causa proxima. Where a loss is brought by several causes in succession to one another, the proximate or nearest cause of loss must be taken into account. If the proximate cause is covered by the policy, only then the insurance company will be liable to compensate the insured.

5. It must contain all the essential requirements of a valid contract, e.g. lawful consideration, free consent, capacity of the parties, etc.

Q25. What are the Principles of Marine Insurance Policy.

Ans :

The following are the key principles of marine insurance policy,

1. Principle of Insurable Interest

The key principle of marine insurance is that the insurer should have interest in the goods being insured. For example, if the cargo reaches safely to the destination port, it is profit for the insured and if the cargo is damaged or destroyed, it is a loss.

In case of marine insurance, the cargo can be sold during the transit of goods. Thus, the insurance policy and the insurable interest would automatically get transferred to the buyer.

Generally, insurable interest is possessed by the following parties,

(a) The ship owner, untill the time the goods are present in his ship.

(b) Passenger have insurable interest in their goods.

(c) The owner of the goods.

(d) Financer who provides money towards the security of the goods.

(e) Individuals who charge freight has insurable interest in that freight.

2. Principle of Implied Warranties

Some aspects of the marine insurance contract are implied and not necessarily need to be specified. Thus, implied warranties are the warranties which are not specifically mention but are to be followed. Example of implied warranties,

(a) Condition of the Ship : Even without being mention, it is an implied warranty that the ship is in a worthy condition. Any repairs if any, need to be carried out before the voyage begins.

(b) Fixed Route : It is implied and assumed by the insurance company that the ship would follow a pre determined route during the voyage.

At times, the ship is deviated from its predetermined routes,

(i) If required to save lives.

(ii) If required for the safety of goods.

(iii) If the ship could not be controlled by the captain.

Q26. Explain the steps for taking a Marine Insurance Policy

Ans :

The first step for initiating a marine insurance policy is for the trader to fill the "Marine Declaration Form (MDF)", which would be available with the insurance provider. The next step is to sign the MDF and submit to the insurance personnel. The MDF would contain the following information,

(i) The proposer individuals name and address.

(ii) Complete details of the cargo to be insured.

(iii) Amount to be insured.

(iv) The voyage period of the marine insurance policy.

(v) Subject matter of insurance policy.

Subject Matter of Marine Insurance

The insured may be the owner of the ship, owner of the cargo or the person interested in freight. In case the ship carrying the cargo sinks, the ship will be lost along with the cargo. The income that the cargo would have generated would also be lost. Based on this we can classify the marine insurance into three categories:

(a) Hull Insurance

Hull refers to the ocean going vessels (ships trawlers etc.) as well as its machinery. The hull insurance also covers the construction risk when the vessel is under construction. A vessel is exposed to many dangers or risks at sea during the voyage. An insurance effected to indemnify the insured for such losses is known as Hull insurance.

(b) Cargo Insurance

Cargo refers to the goods and commodities carried in the ship from one place to another. The cargo transported by sea is also subject to manifold risks at the port and during the voyage. Cargo insurance covers the shipper of the goods if the goods are damaged or lost. The cargo policy covers the risks associated with the transshipment of goods. The policy can be written to cover a single shipment. If regular shipments are made, an open cargo policy can be used that insures the goods automatically when a shipment is made.

(c) Freight Insurance

Freight refers to the fee received for the carriage of goods in the ship. Usually the ship owner and the freight receiver are the same person. Freight can be received in two ways- in advance or after the goods reach the destination. In the former case, freight is secure. In the latter the marine laws say that the freight is payable only when the goods reach the destination port safely. Hence if the ship is destroyed on the way the ship owner will loose the freight along with the ship. That is why, the ship owners purchase freight insurance policy along with the hull policy.

(d) Liability Insurance

It is usually written as a separate contract that provides comprehensive liability insurance for property damage or bodily injury to third parties. It is also known as protection and indemnity insurance which protects the ship owner for damage caused by the ship to docks, cargo, illness or injury to the passengers or crew, and fines and penalties.

Q27. What are the Clauses in a Marine Insurance Policy?

Ans :

A policy of marine insurance may contain several clauses. Some of the clauses are common to all marine policies while others are included to meet special requirements of the insured. Hull, cargo and freight policies have different standard clauses. There are standard clauses which are invariably used in marine insurance. Firstly, policies are constructed in general, ordinary and popular sense, and, later on, specific clauses are added to them according to terms and conditions of the contract.

Some of the important clauses in a marine policy are described below:

1. Valuation Clause

This clause states the value of the subject matter insured as agreed upon between both the parties.

2. Sue and Labour Clause

This clause authorizes the insured to take all possible steps to avert or minimize the loss or to protect the subject matter insured in case of danger. The insurer is liable to pay the expenses, if any, incurred by the insured for this purpose.

3. Waiver Clause

This clause is an extension of the above clause. The clause states that any act of the insured or the insurer to protect, recover or preserve the subject matter of insurance shall not be taken to mean that the insured wants to forgo the compensation, nor will it mean that the insurer accepts the act as abandonment of the policy.

4. Touch and Stay Clause

This clause requires the ship to touch and stay at such ports and in such order as specified in the policy. Any departure from the route mentioned in the policy or the ordinary trade route followed will be considered as deviation unless such departure is essential to save the ship or the lives on board in an emergency.

5. Warehouse to Warehouse Clause

This clause is inserted to cover the risks to goods from the time they are dispatched from the consignor's warehouse until their delivery at the consignee's warehouse at the port of destination.

6. Inchmaree Clause

This clause covers the loss or damage caused to the ship or machinery by the negligence of the master of the ship as well as by explosives or latent defect in the machinery or the hull.

7. F.P.A. and F.A.A. Clause

The F.P.A. (Free of Particular Average) clause relieves the insurer from particular average liability. The F.A.A. (free of all average) clause relieves the insurer from liability arising from both particular average and general average.

8. Lost or Not Lost Clause

Under this clause, the insurer is liable even if the ship insured is found not to be lost prior to the contact of insurance, provided the insurer had no knowledge of such loss and does not commit any fraud. This clause covers the risks between the issue of the policy and the shipment of the goods.

9. Running down Clause

This clause covers the risk arising out of collision between two ships. The insurer is liable to pay compensation to the owner of the damaged ship. This clause is used in hull insurance.

10. Free of Capture and Seizure Clause

This clause relieves the insurer from the liability of making compensation for the capture and seizure of the vessel by enemy countries. The insured can insure such abnormal risks by taking an extra 'war risks' policy.

11. Continuation Clause

This clause authorizes the vessel to continue and complete her voyage even if the time of the policy has expired. This clause is used in a time policy. The insured has to give prior notice for this and deposit a monthly prorate premium.

12. Barratry Clause

This clause covers losses sustained by the ship owner or the cargo owner due to willful conduct of the master or crew of the ship.

13. Jettison Clause

Jettison means throwing overboard a part of the ship's cargo so as to reduce her weight or to save other goods. This clause covers the loss arising out of such throwing of goods. The owner of jettisoned goods is compensated by all interested parties.

14. At and From Clause

This clause covers the subject matter while it is lying at the port of departure and until it reaches the port of destination. It is used in voyage policies. If the policy consists of the word 'from' only instead of 'at and from', the risk is covered only from the time of departure of the ship.

Q28. Explain various types of Marine Losses.

Ans :

A loss arising in a marine adventure due to perils of the sea is a marine loss. Marine loss may be classified into two categories:

1. Total loss

A total loss implies that the subject matter insured is fully destroyed and is totally lost to its owner. It can be Actual total loss or Constructive total loss.

In actual total loss subject matter is completely destroyed or so damaged that it ceases to be a thing of the kind insured. e.g. sinking of ship, complete destruction of cargo by fire, etc.

In case of constructive total loss the ship or cargo insured is not completely destroyed but is so badly damaged that the cost of repair or recovery would be greater than the value of the property saved. e.g. a ship dashed against the rock and is stranded in a badly damaged position. If the expenses of bringing it back and repairing it would be more than the actual value of the damaged ship, it is abandoned.

2. Partial loss

A partial loss occurs when the subject matter is partially destroyed or damaged. Partial loss can be general average or particular average.

General average refers to the sacrifice made during extreme circumstances for the safety of the ship and the cargo. This loss has to be borne by all the parties who have an interest in the marine adventure. e.g. A loss caused by throwing overboard of goods is a general average and must be shared by various parties.

Particular average may be defined as a loss arising from damage accidentally caused by the perils insured against. Such a loss is borne by the underwriter who insured the object damaged. e.g. If a ship is damaged due to bad weather the loss incurred is a particular average loss.

Q29. What are the various types of Marine Insurance Products?

Ans :

The types of marine insurance products :

1. Voyage Policy

It is a policy in which the subject matter is insured for a particular voyage irrespective the time involved in it. In this case, the risk attaches only when the ship starts on the voyage.

2. Time Policy

It is a policy in which the subject matter is insured for a definite period of time. The ship may pursue any course it likes, the policy would cover all the risks from perils of the sea for the stated period of time.

3. Mixed Policy

It is a combination of voyage and time policies and covers the risk during particular voyage for a specified period of time.

4. Valued Policy

It is a policy in which the value of the subject matter insured is agreed upon between the insurer and the insured and it is specified in the policy itself.

5. Open or Unvalued Policy

It is the policy in which the value of the subject matter insured is not specified. Subject to the limit of the sum assured, it leaves the value of the loss to be subsequently ascertained.

6. Floating Policy

It is a policy which only mentions the amount for which the insurance is taken-out and leaves the name of the ship(s) and other particulars to be defined by subsequent declarations. Such policies are very useful to merchants who regularly dispatch goods through ships.

7. Wagering or Honour Policy

It is a policy in which the assured has no insurable interest and the underwriter is prepared to dispense with the insurable interest. Such policies are also known as 'Policy Proof of Interest (PPI)'.

8. Builder's Risk Policy

This policy is issued for more than one year. This covers the risk of damage to vessels from the time its construction commences until its trail is completed.

9. Port Risk Policy

This policy covers all the risk of a vessel while it is standing at a port for particular period of time.

1.5.3 Motor Insurance

Q30. What is motor insurance? Explain the features of motor insurance.

Ans :

Motor insurance is the insurance for motor vehicles, there are various risks which are related with the loss of/or damage to motor vehicles like theft, fire or any accidental damage so as to provide coverage for this motor insurance is taken. Motor insurance is an important part of General Insurance. The rate of premium is standardized because the business is tariff. No insurer can charge lower rates than the tariff rates and no insurer can grant benefits exceeding than those prescribed by the tariff.

Under it, a personal or commercial vehicle is subjected to combined insurance against the risks of :

1. Loss or damage to the motor vehicle and its accessories on account of accident or theft.
2. Death of or injury to the owner or passenger of the vehicle due to accident.
3. Damages payable to third parties by the owner of the vehicle for accident.

A comprehensive insurance policy may be taken to cover all these risks. Insurance against the first two types of risks is optional. But every owner of motor vehicle is required to take out an insurance policy to cover the third party risks under the Motor Vehicles Act, 1956. Such a policy is known as 'third party insurance or liability insurance'. Under such a policy, the third party who has suffered any loss can sue the insurer directly even though that was not a party to the contract of insurance. For example, motor insurance by United India Insurance Company Limited. This policy provides insurance cover to owners of the vehicle, financiers or lessee, who have insurable interest in a motor vehicle.

Motor insurance is an unilateral, executor and conditional contract :

1. Unilateral because it imposes legal duties on only one of the contracting parties, the insurer (insurance company).
2. Executory because the insurer's contractual obligation remains not executed until a loss occurs.
3. Conditional because the insured is also expected to report accidents forward notice of suits, cooperate the insurer, protect damaged property, notify the company in case of loss.

Q31. Explain various types of Motor Insurance Products.

Ans :

To cover the losses arising in respect of motor vehicles, the following different kinds of policies are issued under motor vehicles insurance :

1. Act / Liability Policy

This policy aims at complying with the requirements of Motor Vehicles Act, 1988, and is issued by the insurance companies to cover act risks. The Act provides for compulsory insurance of motor vehicles in relation to liabilities arising out of the use of motor vehicles in a public place. As per the provisions of Motor Vehicles Act, all the vehicles plying in the territorial limits of India must possess an act policy at all times. The violation is punishable with fine, etc., as per Motor Vehicles Act (as prevalent at the time of detection).

The All India Motor Tariff governs motor insurance business in India. According to the tariff, all classes of vehicles use two types of policy forms. They are form A and form B. Form A, or what is commonly known as act policy, covers act liability, which is a compulsory requirement of the Motor Vehicles Act. No vehicle can be used without this minimum insurance cover. Use without such insurance is a penal offense. In case a vehicle is purchased under hire purchase agreement, the financiers insist upon a comprehensive policy to take care of their interest as collateral security.

The following liabilities can be covered under the policy :

i) Unlimited liability towards third party bodily injury.

ii) Liabilities towards damage to the property of third parties. As per requirements of the Motor Vehicles Act, while compensation for personal injuries to third parties is unlimited, property damage is limited (in the case of commercial vehicles it is limited to ` 6,000 only). This limit can be enhanced on payment of additional premium.

iii) Unlimited liability towards bodily injury of passengers of the vehicle.

iv) Liability towards employees of the owner of the vehicle while traveling in or using it, against bodily injury, to the extent required under the Workmen's Compensation Act.

2. Third-Party Policy

This policy provides insurance against the liabilities towards third parties suffering loss pertaining to the damage of property/ personal injury/death. In addition, the policy may also include fire, theft risks, and legal liability to persons employed in connection with the operation and/or maintenance and/ or loading/unloading of motor vehicles. Section 146 of the Motor Vehicles Act 1988, provides that no person shall use or allow any other person to use motor vehicle in a public place, unless the vehicle is covered by the policy of insurance complying with the requirements of the Act. Section 147 of the Motor Vehicles Act 1988, requires that the policy must provide cover against liabilities incurred by the insured in respect of death or bodily injury to any person or damage to any property of a third party or against death or bodily injury to any passengers of a public service vehicle, caused by or arising out of the use of the vehicle in a public place.

3. Package/Comprehensive Policy

Also called form 'B' Policy, the package/ comprehensive policy is an optional policy, which provides cover against own damage, losses, and act liability. It is a package policy issued by the insurance companies for comprehensive risks. Unlike the form AJ Act policy, which is identical for different classes of vehicles, the comprehensive policy cover differs for various classes of vehicles.

Comprehensive policy contains the following three sections :

(i) First section covers damage to the vehicles and covers the risks like fire, explosion, self-ignition and lightning; burglary, house-breaking and theft, riot, strike, malicious and terrorism, damage, earthquake flood, typhoon, etc.

(ii) Second section covers the insured liability to third parties.

(iii) Third section differs according to the class of the vehicles.

Peril which are covered under Motor Insurance Policy

The following perils may be covered under the policy in accordance with the provisions of the tariff :

(i) Damage to vehicle by accidental external means, fire, lightning, explosion, self-ignition, burglary, house-breaking;

(ii) Riot and strike, malicious acts and terrorist acts;

(iii) Earthquake;

(iv) Flood, inundation, cyclone, etc.; and

(v) Landslide/rockslide while in transit by rail, road, air, inland waterways, lift or elevator.

Thus, the policy covers all the risks of liability policy as well as the loss or damage to insured vehicle.

Classification of Motor Vehicles

As per the Motor Vehicles Act for the purpose of insurance the vehicles are classified into three broad categories such as.

1. Private Cars

(a) Private Cars - vehicles used only for social, domestic and pleasure purposes

(b) Private vehicles - Two wheeled

(i) Motorcycle / Scooters

(ii) Auto cycles

(iii) Mechanically assisted pedal cycles

2. Commercial vehicles

(i) Goods carrying vehicles

(ii) Passengers carrying vehicles

(iii) Miscellaneous & Special types of vehicles

Q32. What are the basic Principles of Motor Insurance?

Ans :

Motor insurance being a contract like any other contract has to fulfill the requirements of a valid contract as laid down in the Indian Contract Act 1872. In addition it has certain special features common to other insurance contracts.

They are:

1. Utmost good faith
2. Insurable interest
3. Indemnity
4. Subrogation and contribution

1. Utmost good faith

The principle of Utmost good faith casts an obligation on the insured to disclose all the material facts. These material facts must be disclosed to the insurer at the time of entering into the contract. All the information given in the proposal form should be true and complete e.g. the driving history, physical health of the driver, type of vehicle etc. If any of the mentioned material facts declared by the insured in the proposal form are found inappropriate by the insurer at the time of claim it may result in the claim being repudiated.

2. Insurable Interest

In a valid insurance contract it is necessary on the part of the insured to have an insurable interest in the subject matter of insurance. The presence of insurable interest in the subject matter of insurance gives the person the right to insure. The interest should be pecuniary and must be present at inception and throughout the term of the policy. Thus the insured must be either benefited by the safety of the property or must suffer a loss on account of damage to it.

3. Indemnity

Insurance contracts are contracts of indemnity. Indemnity means making good of the loss by reimbursing the exact monetary loss. It aims at keeping the insured in the same position he was before the loss occurred and thus prevent him from making profit from insurance policy.

4. Subrogation and Contribution

Subrogation refers to transfer of insured's right of action against a third party who caused the loss to the insurer. Thus, the insurer who pays the loss can take up the assured's place and sue the party that caused the loss in order to minimise his loss for which he has already indemnified the assured. Subrogation comes in the picture only in case of damage or loss due to a third party. The insurer derives this right only after the payment of damages to the insured. Contribution ensures that the indemnity provided is proportionately borne by other insurers in case of double insurance.

Q33. Explain various types of Motor Insurance Policies.

Ans :

The All India Motor Tariff governs motor insurance business in India. According to the Tariff all classes of vehicles can use two types of policy forms. They are form A and form B. Form A which is known as Act Policy is a compulsory requirement of the motor vehicle act. Use without such insurance is a penal offence. Form B which is also known as Comprehensive Policy is an optional cover.

1. Liability only Policy

This covers third party liability and / or death and property damage. Compulsory personal accident covers for the owner in respect of owner driven vehicles is also included.

2. Package Policy

This covers loss or damage to the vehicle insured in addition to 1 above.

3. Comprehensive Policy

Apart from the above-mentioned coverage, it is permissible to cover private cars against the risk of fine and / or theft and third party/ theft risks.

Calculation of Premiums

In the case of Comprehensive Insurance Cover, for the purpose of premium, vehicles are categorized as follows:

Private Car

This is used for personal purposes. Private cars are lesser exposed than taxis, as the latter is used extensively for maximum revenue. The premium is computed on the following basis

1. Geographical area of use

Large cities have higher average claim costs followed by suburban areas, smaller cities, and small towns or rural areas. In India, the geographical areas have been classified into Group A and Group B.

2. Cubic Capacity

The more the cubic capacity, the higher the premium rate.

3. Value of the Vehicle

The premium rate is applied on the value of the vehicle. Owner has to declare the correct value of the vehicle to the insurer. This value is known as the Insured's Estimated Value (IEV) in motor insurance and represents the sum insured.

Two-wheeler

It is used for personal purpose only. Premium is calculated on cubic capacity and value of vehicle. Theft of accessories is not covered, unless the vehicle is stolen at the same time.

Commercial Vehicle

This is the vehicle used for hire. For goods carrying commercial vehicle, premium is calculated on the basis of carrying capacity i.e. gross vehicle weight and value of the vehicle. For passenger carrying commercial vehicles, premium is calculated on the basis of again carrying capacity i.e. number of passengers and value of the vehicle. Accessories extra, as specified. Heavier vehicles are more exposed to accidents since the resultant damages they incur are more. Similarly, vehicles with higher carrying capacity expose more passengers to risk. Therefore heavier vehicles attract higher premium rate.

Claim Settlement

Claim arise when

1. The insured's vehicle is damaged or any loss incurred.
2. Any legal liability is incurred for death of or bodily injury
3. Or damage to the third party's property.

The claim settlement in India is done by opting for any of the following by the Insurance company

- Replacement or reinstatement of vehicle
- Payment of repair charges

In case, the motor vehicle is damaged due to accident it can be repaired and brought back to working condition. If the repair is beyond repair then the insured can claim for total loss or for a new vehicle. It is based on the market value of the vehicle at the time of loss.

Motor insurance claims are settled in three stages. In the first stage the insured will inform the insurer about loss. The loss is registered in claim register. In the second stage, the automobile surveyor will assess the causes of loss and extent of loss. He will submit the claim report showing the cost of repairs and replacement charges etc. In the third stage, the claim is examined based on the report submitted by the surveyor and his recommendations. The insurance company may then authorize the repairs. After the vehicle is repaired, insurance company pays the charges directly to the repairer or to the insured if he had paid the repair charges.

Section 110 of Motor Vehicle Act, 1939 empowers the State Government in establishing motor claim tribunals. These tribunals will help in settling the third party claims for the minimum amount

1.5.4 Liability Insurance

Q34. What is liability insurance ? Discuss about liability policies.

Ans :

Meaning

Liability insurance is a mandatory form of insurance for those at risk of being sued by third parties of negligence or other tortuous actions. The regular classes of mandatory policy gives coverage for the ones who provide professional services to the public, for the drivers of vehicles, for those who employ staff and for those who manufacture products which may cause harm.

Liability Policies

The popular liability policies are as follows,

1. **General (Public) Liability Insurance Policy**

   General/Public liability insurance policy is apparently required for every business owner. It provides all-risk protection for any business where the general public deal with legal and medical costs which is due to an incident on its property, even if the insured is not responsible.

2. **Professional Liability Insurance Policy**

   Professional liability insurance policy provides protection for an individual or company in the situation when a client claims that they have experienced a financial loss due to the error or an omission by the individual or company in the delivery of professional services. It is also called as Error and Omissions (E & O) insurance. Professional liability coverage is distinct from a General Liability (GL) policy, which cover majorly for bodily injury or property damage liability. These policies are familiar with healthcare professionals, directors and officers, engineers and other professionals who take cover for liability that arises from their professional negligence.

3. **Product Liability Insurance Policy**

   In the terms of product liability insurance, a product is any physical object which is sold or given away. Product liability is the law area in which distributors, suppliers, retailers, manufacturers and others who make products available to the public are considered responsible for the injuries that occur to the products.

4. **Automobile (Motor) Liability Insurance Policy**

   Automobile/motor liability insurance policy is mandatory in many countries for the automobile owners and users and gives cover for the insured's legal liability to a third party for bodily injury or property damage that is due to negligent operation of an automobile.

5. **Worker's (Workmens) Compensation Policy**

   Workers compensation policy is a type of legally needed insurance given by employers to all employees for work-related illnesses and injuries and also death.

1.5.5 Personal Accident Insurance

Q35. Discuss about Personal Accident Insurance.

Ans : **(Imp.)**

All of us are exposed to the risk of accident, which is a threat to our financial security, and therefore it is prudent to have adequate personal accident cover to manage this contingency. For handling accident risks, personal accident policy, Janata personal accident policy and Gramin personal accident policies are available in India.

Scope of Cover

Personal accident policy pays compensation to the insured in the event of happening of one or more of the following listed below which may be selected by insured at the time of taking policy:

- On death
- On permanent total and partial disability and
- On temporary total disability

In case of accident death during the policy period, the policy in addition covers funeral expenses of the insured person.

Permanent total disablement occurs when an individual is unable to perform his regular duties for the remaining part of his life. Permanent partial disablement may result when a person loses any part of his body due to accident.

When an individual is injured in an accident and as a result he is unable to perform his normal duties for a certain period we can describe it as temporary total disablement. This policy can also be extended to reimburse the medical expenses due to accidents up to 10% of the insured amount or 25% of the claim amount or expenses incurred for treatment of the insured person whichever is less.

Personal accident policy does not cover the injuries resulting out of war, self-inflicted injury, diseases or insanity, death due to war operations, attempted suicides, accident in armed forces, aircraft accidents, accidents due to nuclear weapons etc.

Janata personal accident policy is meant for weaker section of the society. Thus premium charged under this policy is comparatively less. Gramin personal accident policy is designed for the rural people in the country.

It is a contract of Insurance under which the insurer agrees to pay a specific sum of money to the insured in case of bodily injury by accident and to the heirs of the insured in case of death by accident. A contract of personal accident insurance is not a contract of indemnity and the insurer has to pay a fixed sum of money on the death or total disablement of the insured or provide medical benefits for recovery from the injury.

In case of accidental death during the policy period, the policy in addition covers funeral expenses of the insured person. Permanent total disablement occurs when an individual is unable to perform his regular duties for the remaining part of his life. Permanent partial disablement may result when a person loses any part of his body due to accident. It does not cover the injuries resulting out of war, diseases, attempted suicides etc.

Features

To help you understand the features of Personal Accident Policy better we have divided them into two sub-heads:

- **Primary Features**

  Personal Accident Policy is premeditated to offer compensation to an individual or group as per the terms and widely cover accidental demise or impairment (permanent or temporary) the results because of any of these four events:

- **Accidental Death**

  The policy document sets that amount of the money to be paid to a person or his/her dependent that passes away in an accident or sustains serious wounds. Upon producing the necessary documents, one can claim for the amount as per the company process.

- **Permanent Total Disablement**

  In case a person sustains life-long total disablement due to an unfortunate event the advantages/ compensation as per the policy plan is paid to the policyholder.

- **Permanent Partial Disablement**

  The payment, in the case of bodily injuries because of an unfortunate event that results in partial impairment of the policyholder, the compensation is paid as a percentage of the total benefit amount. This percentage may be up to 100% of the benefit amount.

- **Temporary Total Disablement**

  In case a policyholder, due to an accident, sustains some bodily wounds or temporary impairments, a certain fixed amount is paid as a compensation. This can be fixed on the daily or weekly basis and is subject to the maximum limit as per the policy terms.

1.5.6 Specialty Insurance

Q36. What is Specialty Insurance ? Explain various types of Specialty Insurance.

Ans :

Specialty insurance is exactly what it sounds like its insurance that can be purchased for items that are special or unique. Specialty insurance policies are important for items that are not typically covered under other insurance policies. Specialty insurance is necessary for items not covered by your ordinary home owners or automobile insurance. This can include but is not limited to flood coverage, identity theft insurance, mobile home coverage, motorcycle insurance, personal watercraft coverage, boat insurance, pet insurance, private mortgage insurance, travel insurance, title insurance or renters insurance.

Other cases of specialty insurance include insurance for unique items such as actor and actresses who insure their body parts (the ones that are considered their best assets and their money makers), or insurance for a particular project or event that you are spearheading. Specialty insurance for business can also include insuring your entire inventory in case of a fire or theft.

To make the most of specialty insurance basics:

1. Begin by understanding the different types of specialty insurance.
2. Check out various specialties insurance companies.
3. Take a look at the latest specialty insurance coverage and industry news and information.

Specialty Coverage Available

Consider the items you own that are not covered by other insurance policies. For example, what vehicles do you drive that aren't included on your auto insurance policy? What additional coverage is required to protect your home in the event of a flood? Specialty insurance policies should complement your existing auto, home and umbrella policies. An example of these offerings through Ameriprise Auto and Home Insurance and its partners include:

- Antique Vehicles
- ATVs
- Flood insurance for your home or car
- High value homes and rentals
- Motorcycles
- Recreational vehicles
- Watercraft
- Added Protection

Losing a one-of-a-kind item or a unique vehicle to fire or theft or suffering damage in a flood is painful enough. Finding out your insurance doesn't cover the replacement of the item, vehicle or your home or auto would make a heart-breaking situation even worse.

That's why we've developed partnerships with industry leaders in specialty insurance. Our goal is to help you find coverage for these unique items. Through our partnerships, you can purchase insurance policies for a wide range of specialty items.

Types

1. Wedding insurance

It's your big day; you've spent a lot of psychic energy and time planning the special event - not to mention all the money. There are generally two strands of wedding insurance: Cancellation/Postponement and Liability. The first protects your investment in case the wedding is called off or delayed. Liability protects against financial responsibility for guests who get injured while celebrating (read: drinking)

2. Travel Insurance

What's not to love about Paris in the Spring? Needing an emergency root canal in Paris in the Spring. Travel insurance can insure against medical and dental expenses, legal costs, trip cancellations and delays caused by weather. There are also optional/additional aspects of travel insurance that include coverage for higher-risk situations like pre-existing medical conditions, kidnap and ransom - and even specific policies for winter sports enthusiasts.

3. Jet Ski Insurance

Jet Ski insurance is similar to wedding insurance in that it provides protection for the item itself, you the owner, plus anyone else who might use your watercraft. If you're someone who spends a lot of time on a jet ski and hosts a lot of people on your craft Jet Ski insurance may be smart for you, as it protects against such incidents as theft, vandalism, collision, bodily images (to you and/or others), med pay and towing.

4. Jewelry Insurance

Jewelry insurance is included in most homeowner and renter's insurance policies, but only up to certain limit and that limit is usually around Rs. 10,22,000. So if you have a lot of valuable jewelry that you want to protect, jewelry insurance might be a good idea; it will also cover the pieces if you misplace them or if they get harmed in some way. Note that it's also imperative to have the items appraised by a professional, rather than relying purely on personal estimates, especially when emotions are involved. Your grandfather's heirloom bracelet might be your most prized possession (and understandably so) but you want to make sure it has value outside your memories, as you wouldn't want to spend money every month insuring something that the insurance carrier can't or won't replace.

5. Pet Health Insurance

Falling in love with a pet can be a magical experience, lifting one's feet off the ground for days at a time. Unfortunately, we're often brought back down to earth when we receive the first bill from the veterinarian. Pet health insurance is the best way to mitigate against such costs, basically spreading them out across 12 monthly premium payments - instead of getting stuck a huge bill whenever you need to go to the vet.

6. RV insurance

RV insurance is suggested for almost everyone who owns one and most people who rent one. Since the RV is both a home and a vehicle, the insurance industry treats it as such. RV coverage is a blend that protects against collision, weather, vandals, liability and the belongings inside - so you understand why it's so attractive to those who drive such automobiles. It can be an add-on to an existing car insurance policy or purchased separately.

1.5.7 Engineering Insurance

Q37. What is about Engineering Insurance. State the functions of Engineering Insurance.

Ans :

Engineering insurance refers to the insurance that provides economic safeguard to the risks faced by the ongoing construction project, installation project, and machines and equipment in project operation. Depending on the project, it can be divided into construction project all risks insurance and installation project all risks insurance; depending on the attribute of the object, it can be divided into project all risks insurance and machinery breakdown insurance.

Insurance Period: the same as the construction period of the project.

Functions

1. Loss Compensation

Material Loss: The insured project loss caused by any accidents or natural disasters except the exclusions.

The Third Party Liability: According to law, the insured shall assume the compensation liability for the personal injury or property damage to the third party in construction sites and adjacent areas caused by the accident that directly relates to the insured project.

Exclusions: Engineering design, construction technology error, construction material quality defects, mechanical damage of machinery and equipment that happens without external momentum.

2. Special Clause

More than 40 special clauses are available on the basis of risk assessment and payment of additional expenses, including clauses in respect of strike, riot, and civil commotion, limited liability insurance period clause, extended liability guarantee period clause, special fee clause, clause in respect of buildings and tunnels in earthquake region.

3. Target customers

Construction and installation projects in the process of "going out" of construction enterprises, real estate enterprises, production and processing enterprises, electrical power, gas and water production and supply enterprises.

Q38. Explain various types of Engineering Insurance Policies.

Ans :

Several types of engineering insurance policies also combine liability with property insurance. They are :

1. Boiler Insurance Policy

The boiler policy covers for damages to the boiler or other apparatus defined in the schedule to the policy or to the other property of the insured and liability of the insured for injury to third parties or for damage to their property, emerging as a direct result of collapse or explosion of the boiler or other plant mentioned.

2. Engine Insurance Policy

The damages to the engine or machine breakdown is covered by engine insurance policy whereas third party liability and damage to property of insured by flying fragments can be insured if needed. Steam gas, oil and diesel engines, air compressors and refrigerating plant comes in this section.

3. Lifting Machinery Insurance Policy

Lifting machinery and insurance policy is formulated to cover the third party liability and other protection in accordance with the conditions arranged for lifts, cranes, hoists and lifting, passenger and goods.

4. Electrical Plant Insurance Policy

The cover in Electrical Plant Insurance Policy is similar to that of the Engine Insurance Policy and it corresponds to motors, turbo-generators, dynamos and static plant like transformers and rectifiers etc.

Q39. What are the Advantages of Engineering Insurance?

Ans :

1. Winning New Business

Without viable insurance from a company such as, www.catlin.com, it is almost impossible to secure new work and convince potential partners of your quality or attention to detail. This is crucial in a complex and detailed industry such as construction, where even the smallest error or miscalculation can have significant financial implications. By investing in long-term coverage and adapting policies to suit individual projects and work types, you can showcase your diligence as a firm and gain a critical edge in a competitive marketplace.

International projects can greatly benefit your company; however, these need careful planning. Along with bespoke construction differences between countries and cultures, insurance varies dramatically internationally. Just because you're covered in UK, it may be a different story for China, India or Russia.

Making sure you're prepared for this before any opportunities arise will mean you appear a lot more professional when they do.

2. Manage your Long-term Operation Costs

Your long-term operational costs included everything from labour to materials, and a higher level of detail enables you to create and manage your budget more effectively.

So whether you are attending to your firm's overall public liability or organising coverage to suit an individual project, the process of comparing the market and purchasing insurance can deliver a more detailed overview of your financial circumstances. On a final note, this also ensures all future profit and turnover forecasts are accurate.

3. Protect your Business in the Event of Human Error or Misadventure

Arguably the most obvious benefit of purchasing insurance is the fact that it can protect in the event of human error or misadventure.

This protection is primarily financial, whether an employee is injured throughout the course of their work or there are complications with regards to specific projects. So long as you pay careful attention to the individual needs of each project and invest in comprehensive coverage that covers these, you can create a safety net that protects your investment and business reputation.

The construction industry is diverse and unique and this should be reflected in your business approach. Taking a more general attitude towards projects could lead to misunderstanding and complications.

The most successful construction and engineering companies will provide very bespoke projects to meet specific needs. Getting the right insurance for these needs is only the start to ensure you deliver a successful construction campaign.

1.5.8 Other Insurance

Q40. What is Other Insurance? Explain different types of Miscellaneous Insurance Policies.

Ans :

Miscellaneous or other general insurance comprises of different insurance coverages which are prepared to fulfill the unusual requirements of different individuals.

Types

The following are the different types of miscellaneous insurance policies which covers the risks involved in miscellaneous activities,

1. Fidelity Guarantee Insurance

Fidelity guarantee insurance allows an employer to recover his/her losses caused because of dishonesty or disloyalty of employees through dishonest conduct, the insurance company is liable to pay the value to employer on behalf of employees dishonest conduct.

2. Property Insurance

Property insurance is a policy which provide insurance against fidelity, burglary and insolvency. Loss incurred relating to property because of burglary, theft or housebreaking or any other criminal act are covered under property insurance.

3. Building Insurance

Building insurance provide absolute coverage of damage caused to the building of the insured. It is a complete package which cover damages caused by different perils such as lightening, strike, riot, storm, hurricane, flood, etc.

4. Earthquake Insurance

Earthquake insurance was not popular untill the incident of Gujarat few years ago. Earthquake insurance plan cover all the damages caused to the property due to earthquake. The results of Gujarat earthquake were disastrous for every individual who faced financial and personal loss. In this policy, insured is entitled to get complete reconstruction value in the event of loss due to disaster.

5. Flood Insurance

Flood insurance was not so popular in India. The need for flood insurance is observed after experiencing the effects of "tsunami". There is still confusion to categorize under floods or earthquakes as tsunami is a quake in the sea.

6. Burglary Insurance

The Burglary insurance policy covers the losses and damages which are caused to policy holder due to burglary which took place at his/her home, office or at the place mentioned in the policy. The company is supposed to pay for the damages caused due to burglary such as theft of household goods, damage to furniture and so on. Under this type, the maximum amount of loss would be decided during the agreement.

7. Cattle Insurance

Under cattle insurance, animals such as cows, buffaloes, bulls etc are insured. The insurance is provided against the death of animal, which are being kept for the purpose of earning. Policy amount would be decided in accordance to the market value of animal.

8. Engineering Insurance

Engineering insurance is also known as machinery breakdown or plant all risks insurance. This policy provide wide coverage of damages caused to electrical and mechanical machinery. Even the losses suffered by contracts and principals relating to civil engineering projects such as bridges, tunnels, building, etc are covered under this policy.

9. Liability Insurance

In some cases the insured does not incur losses, rather a third person incur losses for certain liability. In such a case the liability insurance is taken from the insurance company. Under which the company is supposed to pay remedy not to the insured but to the party who has incurred losses because of the specified liability.

10. Crop Insurance

Under this type, insurance companies enters into a contract with the farmers to provide them remedy in case of loss or damage to crops by natural calamites. Crop insurance is familiar in countries where agriculture plays a key role in economy.

1.6 Rating and Premiums

Q41. Discuss the concept of rating in general insurance policy.

Ans :

Insurer acts as a rate maker to determine the rate/price of insurance policy. Rate/price of insurance is determined base on the costs involved in production of insurance and future predictions but it is not possible to determine the cost of production for insurance contracts till sales. Rate making is the process of forecasting future losses and expenses of the insurance policies and their distribution among the insured persons. The pricing of other industries differ from insurance companies in the following aspects,

(i) Rate making of an insurance policies depend on the future predictions.

(ii) In insurance policies, rates are influenced by government rules and regulations.

The rates in insurance policies should be adequate, non-discriminatory and does not exceed the limits fixed by the local states. Large companies maintain a separate actuarial department for rate making whereas small companies use the services of actuarial firms. In order to avoid the fluctuations in costs over periods firm should maintain stable rates and these rates should be structured to respond according to the changing conditions and also offer benefits to insured persons.

A price that is characterized by insurer that differ from the premium is called "Rate". Rate should be determined or each unit of production in order to calculate the premium of a policy. Rate differs with the type of insurance, in case of life insurance policies for all the types, premium should be structured in such a way to compensate all the losses and expenses. Premium is determined based on the rates after identifying the expenses and claims involved. Gross premium is the last premium that is paid by the insured and is determined based on gross rate. Gross rate consists of two parts called pure premium to compensate losses and loading to compensate operational expenses.

Pure premium is calculated using the following formula,

$$\text{Pure premium} = \frac{\text{Losses}}{\text{Exposure units}}$$

Gross rate can be calculated using the following relation:

Gross rate = Pure premium + Loading percentage

Loading is the provisions made by the insurer to meet the expenses including commission, acquisition expenses, administrative expenses, allowances for contingencies and profit etc.

$$\text{Gross rate} = \frac{\text{Pure premium}}{\text{Permissible loss ratio}}$$

Permissible loss ratio

$$= 1 - \frac{\text{Expense ratio}}{\text{Loading percentage}}$$

$$GP = PP + LP(GP)$$

$$PP = GP - LP\ (GP)$$

$$PP = GP(1 - LP)$$

$$GP = \frac{PP}{(1 - LP)}$$

Where,

GP = Gross premium

PP = Pure premium

LP = Loading premium.

Q42. Explain various methods of Insurance rating.

Ans :

Rates of insurance policies can be determined using anyone of the following methods:

1. Class rating method
2. Individual rating method
3. Loss ratio method.

Let us explain each method in detail below:

1. Class Rating Method

In this method, the rates are determined uniformly for all the applicants of a group or class irrespective of the other factors such as age, sex of the class etc. The uniform rates assigned to a part of the group are called class rates. This is the simplest method to determine the premiums to each class while determining the class rates, rate maker should consider the credibility of the predictions, number of exposures and the nature of the class (homogeneity is desirable). This method is most commonly used for life and property insurance policies, while estimating the rates makers need to consider the appropriate criteria for classification as in the manual. Hence it is also called manual rate making.

2. Loss Ratio Method

Every time the class rating method does not found appropriate as there exist number of classes and subclasses in a manual. [Losses incurred only on a small exposures dining a period of time], it is not possible to derive a rate for each class. Thus, rate makers are using another method called loss ratio method in which they determine the change in the percentage of the revised rate by comparing the actual loss rate (A) to the expected loss rate (E).

$$\frac{A}{E} = \text{Percentage change in the rate}$$

This change represents the variations in the rates over a period of time. This method is not a rate making method but is a rate revision method.

3. Individual (or) Merit Rating Method

Individual rating method is used to determine the individual risks associated and determine rate to compensate all the risks. Individual rating involves four methods to determine individual rates,

i) Judgement rating

ii) Schedule rating

iii) Experience rating

iv) Retrospective rating.

(i) Judgement Rating : Judgement rating is a method to determine individual rates on a judgement basis. This method includes the procedures of both underwriting and rate making. This method is commonly used for ocean marine insurance and other types of policies. This method is applicable in case of lack of credible statistics and the variations in the exposure units do not leads to construction of a class.

(ii) Schedule Rating : Schedule rating is one of the rating method in which rates are determined based on the schedule/ lists.

Example: Commercial fire insurance.

Rate makers need to consider the factors that has its considerable impact on the probability and severity of loss, credit rates. It is most commonly used in burglary insurance in which rate maker provide credit rates to the loss control devices.

(iii) Experience Rating : In this method, insurer determine the premium based on the past experience of insured in losses. Rate is determined as in class rating system but the premium has been adjusted based on the degree of deviation of insured's experience from the average class experience. This method is most commonly used for insurance policies with high premium and insurance of worker's compensation, general insurance, life and health insurance etc. Insurer needs to determine the percentage of change in the actual loss from the expected and modify the percentage with credibility factor. The resulting figure represents the credit/debit of the premium. In general the average experience period is three years and rate makers are required to determine the loss ratio using three year average method.

Credibility factor represents the degree of confidence in predicting future experience based on past experience. The creditability factor depends on the quantity of losses in past period of experience.

$$\text{Modification} = \frac{\text{ALR} - \text{ELR}}{\text{ELR}}$$

Where,

ALR = Actual loss ratio

ELR = Expected loss ratio.

(iv) Retrospective Method : This method is a self rated and cost plus method in which premium can be determined by considering the actual loss experience by the insured in the present policy period instead of future periods. Actual loss can be calculated by establishing a premium deposit at the policy inception and then alter the premium at the end of the policy period. The premium at the end of the period consists of fixed charge, actual losses, adjusted charges and loading percentage.

Q43. Define insurance premium. What are the factors based on which insurance premium is fixed ?

Ans :

The price paid by the policy holder for the insurance policy is referred as insurance premium. The Premium is a regular payment which is paid by the insured either monthly, quarterly, half-yearly or annually depending upon the terms and conditions in the Insurance contract. In case, if premium is not paid then the policy would lapse and revival of policy is possible only be supposed to pay certain percentage of Interest on it. The Rate of premium differs from one policy to another depending on the nature of policy and particulars of the insured.

Factors

Fixing of premium refers to the process of fixing insurance premium rate of different life and non-life risks, the process of fixing life insurance premium rate is based on the following factors,

1. Age of Person

Age of the person is the most common factors which effects the rate of life insurance premium. If a person is young then the premium rate would be lower and if he is old the premium rate will be higher. The reason behind such difference is that the probability of having life threatening diseases or death to a young person is very less compare to the old person.

2. Gender of Person

Insurance companies are not against the gender of a person but they discriminate the gender based on the importance of life of men and women. According to an research study, women's may live 5 years more than mens. As a result women will pay premium for larger period but at lower rate which is a plus point for women's.

3. Smoking Persons

The smoking factor have direct influence on the premium rates. The premium rates of smokers are usually doubled compare to non-smokers. Because smokers always have high risk of suffering from any life threatening diseases.

4. Health Record of Persons

Health record of persons helps to reduce the premium rates. Insurance companies provide insurance coverage based on the health records submitted by the insurance policy holder. Thus, health records also effect the fixation of premium rates.

5. Drinking

As every one knows that consuming alcohol is injurious to health, insurance companies also knows this and due to which they take the advantages of this reason. They will charge high premium rates for the policy holders who have the habit of alcohol drinking.

6. Policy Tenure

The tenure of the insurance policy, directly effect the rate of insurance premium. Because larger the tenure, larger will be the amount of benefits received at the time of death.

7. Profession of Persons

Profession of persons is another factor which may effect the premium rates of life insurance policy. The profession of persons increases of decreases the amount of premium, i.e. the persons who are working in mining industry like oil, gas, fisheries etc. are considered as the persons whose life is in danger. This probability of meeting with an life ending accidents with such persons is more compare to the persons who are working in a standard BPO office.

Thus the above factors effects the rate of insurance premium but their effect is dependent on the nature of risk involved and consideration of factors according to insurance companies.

Q44. Explain about IRDA and reserve for unexpired risk along with its treatment.

(OR)

Discuss about Insurance Regulatory and Development Authority.

Ans : **(Imp.)**

In 1996, Insurance Regulatory Authority (IRA) was formed by government with an aim to monitor and control the operations of the insurance business. Later on, the name of this authority was changed to 'Insurance Regulatory and Development Authority (IRDA) which formulated the rules and regulations for preparing the Financial Statements of insurance companies in the year 2002. In these regulations, schedules (I, II, III) which were specified in the Insurance Act, 1938 are being excluded and the formats for preparing the Revenue Account, Profit and Loss Account and Balance Sheet of insurance companies are included.

Reserve for Unexpired Risk

Reserve for unexpired risk is the premium concerning the general insurance business which is received in advance by insurance company. The duration of general insurance policies is 1 year and it must be renewed every year. In general insurance, policies can be issued at any time in the year and majority of the policies are found active even after the end of the financial year. As risk may take place on any day before the expiry of 1 year provisions must be made to fulfill the claims which may take place after the end of financial year. Hence, this provision is known as “reserve for unexpired risk”.

As per section 64 V(i) (ii) (b) of IRDA Act, in case of marine insurance, the reserve for unexpired risk must be 100% of the net premium whereas the provision for unexpired risk must be 50% of net premium of the marine insurance and other insurance businesses like fire, theft, accident, etc.

Accounting Treatment

Any adjustment relating to change in reserve for unexpired risk must be disclosed in schedule 1 - premium earned (Net). Calculation and accounting treatment of net premium is as follows,

1. Ascertain the difference between closing reserve for unexpired risk and additional reserve and opening reserve for unexpired risk and additional reserve.
2. If the amount of closing reserves exceed the amount of opening reserves then the difference amount has to be subtracted from the premium earned.
3. If the amount of opening reserves exceed the amount of closing reserves then the difference amount has to be added to the premium earned.

After making the adjustments, the net premium must be taken in revenue *a/c* as “premium earned (Net)”. The closing balance of reserve for unexpired risk must be covered under schedule 14- provision for balance sheet purpose. The balance of provision is shown on the liabilities side of balance sheet under the heading “balance of funds and accounts”.

Q45. What are the features of IRDA ?

Ans :

The following are salient features of the IRDA Act (1999),

1. The insurance sector in India has been thrown open to the private sector. The second and third schedules of the act provide for removal of existing corporations (or companies) to carry out the business of life and general (non-life) insurance in India.
2. An Indian insurance company is a company registered under the Companies Act, 1956, in which foreign equity does not exceed 26 percent of the total equity shareholding, including the equity shareholding of NRIs, FIIs and OCBs.
3. After commencement of an insurance company, the Indian promoters can hold more than 26 percent of the total equity holding for a period of ten years, the balance shares being held by non-promoter Indian shareholders which will not include the equity of the foreign promoters and the shareholding of NRIs, FIIs and OCBs.
4. After the permissible period of ten years, excess equity above the prescribed level of 26 percent will be dis invested as per a phased programme to be indicated by IRDA. The central government is empowered to extend the period of ten years in individual cases and also to provide for higher ceiling on share holding of Indian promoters in excess of which disinvestment will be required.
5. On foreign promoters, the maximum of 26 percent will always be operational. They will thus be unable to hold any equity beyond this ceiling at any stage.
6. The act gives statutory status for the Interim Insurance Regulatory Authority (IRA) set up by the central government through a resolution passed in January 1996.
7. All the powers presently exercised under the Insurance Act, 1938, by the Controller of Insurance (CoI) will be transferred to the IRDA.
8. The IRDA act also provides for the appointment of CoI by the central government when the regulatory authority is superseded.

9. The minimum amount of paid-up equity capital is Rs. 100 crores in case of life insurance as well as general insurance and Rs. 200 crores in the case of reinsurance.

10. Solvency margin (excess of assets over liabilities) is fixed at not less than Rs. 50 crores for life as well as general insurance, for reinsurance solvency margin is stipulated at not less than Rs. 100 crores in each case.

11. Insurance companies will deposit Rs. 10 crores as security deposit before starting their business.

12. In the non-life sector, IRDA would give preference to companies providing health insurance.

13. Safeguards for policy holders' funds include specific provision prohibiting investment of policy holders' funds outside India and provision for investment of funds in accordance with policy directions of IRDA, including social and infrastructure investments.

14. Every insurer shall provide life insurance or general insurance policies (including insurance for crops) to the persons residing in the rural sector, workers in the unorganised or informal sector or for economically vulnerable or backward classes of the society and other categories of persons as may be specified by regulations made by IRDA.

15. Failure to fulfill the social obligations would attract a fine of Rs. 25 lakhs, in case the obligations are still not fulfilled, licence would be cancelled.

Q46. What are the duties and responsibilities of IRDA?

Ans :

Under Section 14 of the IRDA Act, the authority's duty is to regulate, promote and to ensure an orderly growth of the insurance and the re-insurance business.

Under sub-Section 1 of Section 14 of the IRDA Act, the authority has the following duties and responsibilities :

1. Registration

Issuance of certificate of registration, or to renew, modify, withdraw, suspend or cancel such registration.

2. Protection

Protection of the interests of policy holders in matters concerning assigning of policy, nomination by policy holders, insurable interest, settlement of insurance claim, surrender value of policy and other terms and conditions in contracts of insurance.

3. Qualification

Specifying the requisite qualifications, code of conduct and practical training for insurance intermediaries and agents.

4. Code of Conduct

Specifying the code of conduct for surveyors and loss assessor.

5. Efficiency

Promoting efficiency in the conduct of the insurance business.

6. Professionalism

Promoting and regulating professional organizations connected with the insurance and re insurance business.

7. Fees

Levying fees and other charges for carrying out the objectives of this act.

8. Information

Calling for information from, undertaking inspection of, and conducting enquiries and investigations, including audit of the insurers, intermediaries, insurance intermediaries and other organizations connected with the insurance business.

9. Terms of Business

Control and regulation of the rates, advantages, terms and conditions that may be offered by insurers for general insurance, business not so controlled and regulated by the Tariff Advisory Committee under Section 64U of the Insurance Act, 1938 (4 of 1938).

10. Books of Accounts

Specifying the form and the manner in which books of account shall be maintained, and statement of accounts shall be rendered by insurers and other insurance intermediaries.

11. Funds Investment

Regulating investment of funds by insurance companies.

12. Margin of Solvency

Regulating the maintenance of margin of solvency.

13. Adjudication

Adjudication of disputes between insurers and intermediaries or insurance intermediaries.

14. Supervising

Supervising the functioning of the Tariff Advisory Committee.

15. Premium Income

Specifying the percentage of the premium income going into finance schemes for promoting and regulating professional organizations pursuing assurance business.

16. Rural and Social Insurance

Specifying the percentage of life insurance business and general insurance business to be undertaken by the insurer in the rural or social sector.

17. Others

Exercising other powers as may be prescribed.

1.7 Concept of Soft and Hard Markets

Q47. Explain briefly about Soft and Hard Markets in general insurance.

Ans : **(Imp.)**

(i) Soft Markets

Soft Market is a market that has more potential sellers than buyers. A soft market can describe an entire industry, such as the retail market or a specific asset, such as lumber. This is often referred to as a buyer's market, as the purchasers hold much of the power in negotiations.

A soft market can lead to rapid drops in prices as sellers compete to find buyers. Prices will fall as the excess of supply over demand increases. For example, assume that 20 houses are put up for sale and 15 possible buyers enter the market. Five of these houses will not be sold, assuming each buyer purchases one house. This forces the 20 house sellers to compete on price in order to attract a buyer. As a result, this type of housing market would be called soft.

Characteristics

A soft market is characterized by the following:

(a) Many insurers are competing for business.

(b) Coverage is widely available.

(c) Insurance prices are low.

(d) Underwriters are flexible and willing to negotiate coverage terms.

(e) Broad coverage is available with some extensions available for free.

(f) Underwriting standards are relaxed.

(ii) Hard Markets

Hard market is the situation where demand is high but supply is low, therefore sellers can dictate prices to maximize their returns.

Characteristics

A hard insurance market is opposite of a soft one. Here are the characteristics of a hard market:

(a) Relatively few insurers are offering coverage

(b) Coverage is difficult (or even impossible) to obtain

(c) Insurance prices are high

(d) Underwriters are reluctant or unwilling to negotiate coverage terms

(e) Broad coverage is difficult to obtain. Some extensions may be available for an additional premium.

(f) Underwriting standards are strict.

Short Question and Answers

1. Define Life insurance.

Ans :

Meaning

The life insurance contract provide elements of protection and investment after getting insurance, the policyholder feels a sense of protection because he shall be paid a definite sum at the death or maturity. Since a definite sum must be paid, the element of investment is also present. In other words, life insurance provides against pre-mature death and a fixed sum at the maturity of policy. At present, life insurance enjoys maximum scope because each and every person requires the insurance.

Life insurance is a contract under which one person, in consideration of a premium paid either in lump sum or by monthly, quarterly, half yearly or yearly installments, undertakes to pay to the person (for whose benefits the insurance is made), a certain sum of money either on the death of the insured person or on the expiry of a specified period of time.

Definitions

(i) **According to J.H Maggee,** life insurance can be defined as "the life insurance contracts embodies an agreement in wkich the insurer undertakes to pay a stipulated sum upon the death of the insured or at designated time to a designated beneficiary.

(ii) **According to the section 2** of Indian insurance Act, 1938 "Life Insurance business is the business effecting contracts upon human life".

2. Define premium.

Ans :

Premium is an amount paid periodically to the insurer by the insured for covering his risk.

In an insurance contract, the risk is transferred from the insured to the insurer. For taking this risk, the insurer charges an amount called the premium. The premium is a function of a number of variables like age, type of employment, medical conditions, etc. The actuaries are entrusted with the responsibility of ascertaining the correct premium of an insured. The premium paying frequency can be different. It can be paid in monthly, quarterly, semiannually, annually or in a single premium.

3. Define Rebate. State the various modes of Rebates.

Ans :

Meaning

Rebate is the amount paid for reduction, return or refund on what has been already contributed or paid. In a insurance policy, rebates can be of different types like, yearly, half-yearly, quarterly and monthly. Rebates are usually differ from plan to plan. It is very important to deduct permissible rebate for mode of payment of premium and sum assured for insurance.

Mode of Rebates

There are four types of modes of rebates which are used in the calculation of insurance premium. They are as follows,

(i) Yearly mode of rebates

(ii) Half yearly mode of rebate

(iii) Quarterly mode of rebate

(iv) Monthly mode of rebate.

When the premium are paid on yearly or half-yearly basis, then there will be saving of administrative expenses compared to quarterly mode of rebate. In yearly and half-yearly modes, the insurer issues less number of notices, collection receipts and consequential entries. Thus, administrative cost get reduced. However, in monthly mode, the extra premium is to be charged by insurer to cover additional administrative expenses.

This is summarised below,

(i) When less number of premium installment are there, then higher will be the amount and more will be the f& discount.

(ii) When more number of premium installment are there, then less will be the amount and discount.

Premium

$$= \text{Sum Assured} \times \frac{\text{Rate of Premium}}{1000}$$

However the mode of rebate (Payments) for yearly, half-yearly, quarterly and monthly are listed below,

(i) Yearly - 3% less than the table rate

(ii) Half-yearly - 1.5% less than the table rate

(iii) Quarterly - Nil

(iv) Monthly - 5% more than the table rate (it is to be added).

4. What is loading and premium loading?

Ans :

(i) Loading

Loading is the costs of an insurance policy. It is a type of cost which includes selling and administrative costs like, marketing cost, employees salaries, cost associated with brokers, agents and premium taxes. Cost of capital is also one of the component of loading which is more difficult to understand.

The cost of capital is a kind of reserves which enable the insurance company (insurer) to pay unexpected by higher claims. In this case, loading include a amount which covers the transactions costs associated with making these assets available to insurance company. Addition to this, it also include higher tax cost to the investor associated with such investment. The loading is usually expressed in percentages of premium, which is referred as premium loading factor.

(ii) Premium Loading

The premium loading refers to the margin which is require by a insurance company (Insurer) for covering up the overhead expenses and generating appropriate profit. It is calculated by using following formula,

Premium Loading Factor

$$= 1 - \frac{\text{Expected loss}}{\text{Premium}}$$

5. Rider Premium

Ans :

The extra premium paid to receive extra benefit from insurance policy is known as rider premium. Extra premiums are usually paid to compensate the extra risk or to secure extra disability or death benefits. The rider premium will be added after the calculation of actual premium. It is the last factor which is to be added in premium amount for availing extra benefits.

Benefits

Following points highlights the benefits of riders,

(i) It increases the value of the insurance policy.

(ii) It can be availed only if the insurance premium for the basic benefits is being paid.

(iii) It will be stopped when basic premium of sum assured get stopped.

(iv) In some cases, it can be availed upto certain age of the insured.

(v) It can be added to the insurance policy from the Date of Commencement (DOC) of the policy.

(vi) It also can be added from the policy anniversary based on the Date of Application (DOA).

6. What is Surrender Value?

Ans :

The term surrender value refers to the amount of money which the insurer agrees to pay in case the life assured decides to surrender his policy before its maturity. It is said that the policyholder wishes to surrender his policy to the insurer and gives up his claim on it. Surrender of policy indicates termination of the contract of insurance.

The amount of surrender value is determined on the basis of actual premium paid and the number of years the policy has been in force. Surrender value increases with each payment of premium. Payment is to be made against the full and final discharge of insurer's liability under the contract.

7. Cover Note

Ans :

A cover note is a document issued in advance of the policy. It is issued when the policy cannot for some reason or the other, be issued straight away. Cover notes are issued when the negotiations for insurance are in progress and it is necessary to provide cover on a provisional basis or when the premises are being inspected for determining the actual rate applicable. Pending the preparation of the policy, the cover note is issued as evidence of protection for a temporary period of time and to prove that cover is in force. Here is a brief detail of cover.

In Marine Insurance, marine cover notes are normally issued when details required for the issue of policy such as name of the steamer, number of packages or exact value etc. are not known. In Fire Insurance,, the operative clause of a fire cover note is issued in consideration of the proposer named in the schedule having proposed the effect of an insurance against fire for the period mentioned, on the usual terms and conditions of the company's policy. In Motor Vehicle Insurance, motor cover notes are to be issued in the form prescribed by the Motor Tariff.

8. Proposal Forms

Ans :

The company's printed proposal form is normally used for making an application for the required insurance cover. The proposal form contains questions designed to elicit all material information about the particular risk proposed for insurance. The number and nature of questions vary according to the particular class of insurance covered.

In Marine Cargo Insurance, Insurance document is not the practice to use a proposal form, although sometimes it is usual to obtain a questionnaire or a declaration form duly completed. Proposal forms are used for hull insurance.

In Fire Insurance, the practice varies among the companies, proposal forms are not generally used for large industrial risks where inspection of the risk is arranged before acceptance of the risk. Forms are used for simple risks. Proposal forms are used in respect of risks which are normally declined but have to be accommodated to retain the goodwill of the client.

In Miscellaneous Insurance, proposal forms are invariably required and they incorporate a declaration which extends the common law duty of good faith. Fire proposal forms may or may not have the declarations. The following items may be considered as common to all proposal forms.

- Proposer's name in full
- Proposer's address
- Proposer's profession, occupation or business
- Previous and present insurance
- Loss experience
- Sum insured
- Other Section's - Signature, date, place etc.

9. What is Fire Insurance ?

Ans :

Fire insurance provides protection against damage to property caused by accidents due to fire, lightening or explosion, whereby the explosion is caused by boilers not being used for industrial purposes. Fire insurance also includes damage caused due to other perils like storm, tempest or flood, burst pipes, earthquake, aircraft, riot, civil commotion, malicious damage, explosion, etc.

Section 2 of the Insurance Act 1938 defines fire insurance as "The business of effecting, otherwise than incidentally to some other class of insurance business, contract of insurance against loss by or incidental to fire or other occurrence customarily included among the risks insured against in fire insurance policies".

10. What is marine insurance ?

Ans :

Marine insurance basically covers three risk areas, namely: hull, cargo and freight. The risks which these areas are exposed to are collectively known as "Perils of the Sea". These perils include theft, fire, collision, etc. Section 2(13)A of the Insurance Act 1938 defines marine insurance as, "Marine insurance business" means the business of effecting contracts of insurance upon vessels of any description, including cargoes, freights, and other interests which may be legally insured in or in relation to such vessels, cargoes and freights, goods, wares, merchandise and property of whatever description insured for any transit by land or water or both, and whether or not including warehouse risks or similar risks in addition or as incidental to such transit and includes any other risks customarily included among the risks insured against in marine insurance policies.

11. What is motor insurance?

Ans :

Motor insurance is the insurance for motor vehicles, there are various risks which are related with the loss of/or damage to motor vehicles like theft, fire or any accidental damage so as to provide coverage for this motor insurance is taken. Motor insurance is an important part of General Insurance. The rate of premium is standardized because the business is tariff. No insurer can charge lower rates than the tariff rates and no insurer can grant benefits exceeding than those prescribed by the tariff.

12. Define insurance premium.

Ans :

The price paid by the policy holder for the insurance policy is referred as insurance premium. The Premium is a regular payment which is paid by the insured either monthly, quarterly, half-yearly or annually depending upon the terms and conditions in the Insurance contract. In case, if premium is not paid then the policy would lapse and revival of policy is possible only be supposed to pay certain percentage of Interest on it. The Rate of premium differs from one policy to another depending on the nature of policy and particulars of the insured.

13. IRDA

Ans :

In 1996, Insurance Regulatory Authority (IRA) was formed by government with an aim to monitor and control the operations of the insurance business. Later on, the name of this authority was changed to

'Insurance Regulatory and Develop-ment Authority (IRDA) which formulated the rules and regulations for preparing the Financial Statements of insurance companies in the year 2002. In these regulations, schedules (I, II, III) which were specified in the Insurance Act, 1938 are being excluded and the formats for preparing the Revenue Account, Profit and Loss Account and Balance Sheet of insurance companies are included.

14. What are the features of IRDA ?

Ans :

(i) The insurance sector in India has been thrown open to the private sector. The second and third schedules of the act provide for removal of existing corporations (or companies) to carry out the business of life and general (non-life) insurance in India.

(ii) An Indian insurance company is a company registered under the Companies Act, 1956, in which foreign equity does not exceed 26 percent of the total equity shareholding, including the equity shareholding of NRIs, FIIs and OCBs.

(iii) After commencement of an insurance company, the Indian promoters can hold more than 26 percent of the total equity holding for a period of ten years, the balance shares being held by non-promoter Indian shareholders which will not include the equity of the foreign promoters and the shareholding of NRIs, FIIs and OCBs.

(iv) After the permissible period of ten years, excess equity above the prescribed level of 26 percent will be dis invested as per a phased programme to be indicated by IRDA. The central government is empowered to extend the period of ten years in individual cases and also to provide for higher ceiling on share holding of Indian promoters in excess of which disinvestment will be required.

Choose the Correct Answer

1. Which one of the following does not belong to the main products of life insurance? [d]
   - (a) Term
   - (b) Whole life
   - (c) Endowment
   - (d) Personal accident insurance
2. Which one of the following does not belong to the major general insurance private sector companies in India? [b]
   - (a) Reliance General Insurance
   - (b) The Oriental Insurace Company
   - (c) Bajaj Allianz General Insurance
   - (d) Royal Sundaram Alliance Insurance
3. When was Life Insurance sector nationalised? [c]
   - (a) 1947
   - (b) 1951
   - (c) 1956
   - (d) 1959
4. When was the General Insurance Council formed? [c]
   - (a) 1955
   - (b) 1956
   - (c) 1957
   - (d) 1958
5. When was the Insurance Regulatory and Development Authority constituted? [b]
   - (a) 1971
   - (b) 1999
   - (c) 2001
   - (d) 2005
6. IRDA stands for. [b]
   - (a) Indian Rural Development Authority
   - (b) Insurance Regulatory and Development Authority
   - (c) Insurance Rural Development Authority
   - (d) Insurance Revenue Development Authority
7. provide the benefit to insured to claim from the insurer any loss incurred due to the negligence of third party. [c]
   - (a) Principle of utmost good faith
   - (b) Principle of contribution
   - (c) Principle of subrogation
   - (d) Principle of indemnity
8. The amendments made by IRDA in which of the following acts, [c]
   - (a) GICAct, 1972
   - (b) LIC Act, 1956
   - (c) Both (a) and (b)
   - (d) MRTP Act
9. The main purpose of is to prevent gambling and minimize the moral hazard. [c]
   - (a) Subrogation
   - (b) Utmost good faith
   - (c) Insurable interest
   - (d) Proximate cause
10. The facts that should not be disclosed by insured are, [d]
   - (a) Facts that minimize the risk
   - (b) Facts relating to public knowledge
   - (c) Facts waived by insurer
   - (d) All the above

11. The general insurance Corporation of India was incorporated as a company in the year [b]
    (a) 1970 (b) 1971
    (c) 1972 (d) 1973

12. The amendments made by IRDA in which of the following acts, [c]
    (a) GIC Act, 1972 (b) LIC Act, 1956
    (c) Both (a) and (b) (d) MRTP Act

13. Which one of the following is not a function of insurer? [d]
    (a) Production (b) Underwriting
    (c) Rate making (d) None of the above

14. IRDA stands for ________. [b]
    (a) Indian Rural Development Authority
    (b) Insurance Regulatory and Development Authority
    (c) Insurance Rural Development Authority
    (d) Insurance Revenue Development Authority

15. Different types of motor vehicle insurance policies are [d]
    (a) Act policy (b) Collision insurance policy
    (c) Garage insurance policy (d) All the above

16. Health insurance is basically divided into two types, disability income insurance and ________. [b]
    (a) Participating life insurance (b) Medical expense insurance
    (c) Adjustment life insurance (d) None of the above

17. The legal right to insure arising out of a financial relationship recognized under the law between the insured and the subject matter of insurance is called [a]
    (a) Principle of insurable interest (b) Principle of utmost good fait
    (c) Principle of subrogation (d) Principle of indemnity

18. ________ decide whether to accept or to reject the insurance proposal. If the proposal is accepted at what price it should be accepted [d]
    (a) Agent (b) Intermediaries
    (c) Actuaries (d) Underwriters

19. Reinstatement policy is also called ________. [a]
    (a) Replacement policy (b) Recurrence policy
    (c) Instalment policy (d) Renew policy

20. Insurance which is not covered under other insurance policies comes under [b]
    (a) Fire insurance (b) Speciality insurance
    (c) Accident insurance (d) Marine insurance

Fill in the blanks

1. LIC stand for ________
2. PLI stand for ________
3. ULIPs stand for ________
4. Example of LIC plan ________
5. Type of Health insurance ________
6. ________ is the pooling of for feitous losses by the transfer of risk of insured to insurer.
7. The process of identification and classification of the risks involved in insurance program is called ________
8. The price paid by the policy holder for the insurance policy is referred as ________.
9. The insurance that pays death benefits to the beneficiaries after the death of the insured is known as ________
10. IRDA plays a role of a ________ for the insurance industry in India.
11. IRDA plays a role of a ________ for the insurance industry in India.
12. Insurer can be a ________.
13. Insurance emerged in India during ________ century.
14. ________ is also called as non-life insurance.
15. ________ help with insurance approvals at the time of cashless admission in the hospital and with settling the bill with the insurer on discharge.
16. The State Bank of India enter into a joint venture agreement with ________ for undertaking general insurance business.

ANSWERS

1. Life Insurance Corporation
2. Postal Life Insurance
3. Unit linked policy
4. Money Back policy
5. Group Health Insurance
6. Insurance
7. Underwriting
8. Premium

9. Life insurance
10. Regulator
11. Regulator
12. Company or Person
13. 18^{th}
14. General Insurance
15. Third Party Administrators
16. Insurance Australia Group

UNIT II

Settlement of Claims Risk & Underwrittings and Financial Planning & Tax Saving:

Life Insurance: Settlement of claims: Intimation Procedure, documents and settlement procedures - Underwriting: The need for underwriting - Guiding principles of Underwriting - Factors affecting Insurability – Methods of Life Classification - Laws affecting Underwriting - Financial Planning and taxation: Savings - Insurance vis-à-vis- Investment in the Units Mutual Funds, Capital Markets - Life Insurance in Individual Financial Planning – Implications in IT treatment.

General Insurance: Concept of Underwriting - Underwriting Process - Risk sharing and its methods - risk management and steps involved in it - Concept of Claim - understanding the process of claim management - claims fraud and fraud prevention - Insurance reserves and accounting - different types of reserves of insurance companies - reserving process followed by insurance companies - Insurance accounting.

2.1 Settlement of Claims: Intimation Procedure, Documents and Settlement Procedures

Q1. Define claim? What are the different types of Life insurance Claims?

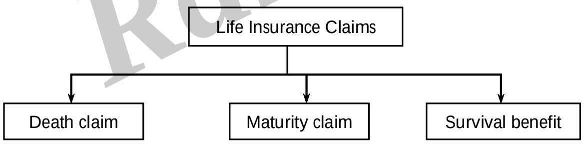
Ans : **(Imp.)**

Meaning

Claim refers to the demand made by an insured or beneficiary to the insurer to make payment of insurance policy benefits

Types

The insurance claims are divided into three types.



The basic necessity for settlement of claim arises on death of the policy holder or maturity of policy.

A) Death Claim

The death claim arises on the death of the policy holder. Death can be natural, accidental or a suicide. Death claim is further classified as,

(i) Premature Claim

In case of premature claim, insured person dies within three (3) years from the date on which insurance policy is taken.

(ii) Other Claim

In case of other claim, insured person dies after three (3) years from the date on which insurance policy is taken.

B) Maturity Claim

The essential features of maturity claims are listed below,

1. A maturity claim is payable according to the conditions of the contract on the completion of the policy term period, if the insured person is alive till the maturity date.
2. This claim includes the assured sum, vested bonuses and other specified money. Any debt or charge under the policy such as outstanding premia and loans will be deducted from the assured sum.
3. When it comes to proof of title, settlement of maturity claims is quite easy as the policy money is paid directly to the insured person itself.
4. The insurance company will make payment to the absolute assignee in case of an absolute assigned policy.
5. Policy holders are informed in advance about the maturity date by the insurers. The insurers also send the discharge form to the policy holders and request them to return the discharge form signed, duly stamped and enclosed with the documents such as,

(i) The policy document

(ii) Age proof (if age is not admitted yet)

(iii) In case if an assignment is made, the stamped document of assignment should also be submitted.

C) Survival Benefit

Some policies such as money back policies allow the insured person for the survival benefit before the full term policy expires. Settlement of the survival benefit is less complicated when compared to settlement of maturity claim.

The procedure for settlement of survival benefit is as follows,

1. Insurer intimates the policy holder in advance about the money back policies and sends a discharge voucher.
2. The policy holder returns the documents duly stamped and signed and witnessed with the original policy document for necessary approval.
3. The gross amount is nothing but the installments of the sum of money assured payable.
4. After subtracting the outstanding premium, outstanding loan, interest etc., from the gross amount, the net amount will arrive.

Q2. What do you mean by claim settlement? Explain the procedure for claim settlement for life insurance policies.

(OR)

Explain the procedure in claim settlement on maturity of insurance policies.

(OR)

What is claim settlement? Explain the procedure in claim settlement on maturity of insurance policy.

(OR)

What is claim settlement? Explain the procedure for settlement of claim.

Ans : **(Imp.)**

Claim settlement means paying back the money by the insurance company to the insurance policy holder. A claim is said to be settled when the policy holder duly receives the money which is due to him by the company according to the terms and conditions of policy. The process of claim settlement directly reflects the efficiency and effectiveness of the company. A company which correctly and successfully settles down the claims of clients achieves trustworthiness and loyalty. While the insurance companies which involve litigations in claim settlements owes bad reputation in the market.

Claim settlement of an insurance policy usually takes place in two circumstances,

A) On death of policy holder.

B) On maturity of insurance policy.

A) Procedure for Settlement of Claim on the Death of Policy Holder

In case of death of policy holder, the following procedure is followed and the claim is settled down,

1. Intimation of Death

The process of claim settlement basically starts with intimating about the death of policy holder (insured) to the respective office of LIC from where the policy was being purchased. The intimation letter should include the following details, full name of the insured, policy number, date and place of death and so on. The letter must be forwarded by the correct nominee, assignee or the close relative of policy holder. The relationship between the person sending the intimation letter and the insured should also be mentioned.

2. Filling Forms of Claim

Soon after receiving the intimation letter, the official authorities would send certain claim forms to the nominee. These forms need to be duly filled up in a prescribed format and should be returned back to the authorities within the specified time period.

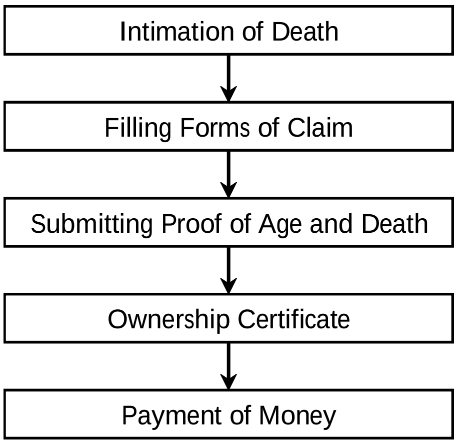


Figure: Procedure for Settlement of Claim on Death of Policy Holder

3. Submitting Proof of Age and Death

In addition to sending letter of death intimation and filled up forms, it is also required to submit the proof of age and death to the concerned officials. For submitting the proof of age, school certificate, birth certificate or citizenship card might be used. And for proof of death, death certificate from hospital or from municipality might be submitted. If necessary, it is also required to submit the statement of doctor who was giving treatment to the insured and the certificate from hospital in which the insured got treatment for the illness.

4. Ownership Certificate

Certificate of ownership is needed in case when there is no valid nominee or assignee mentioned in the policy. It can be a succession certificate, letters of probate and the similar kind.

5. Payment of Money

After successfully completing all the steps, the money is paid to the right person i.e., nominee. The LIC company sends a cheque in the name of nominee which can be withdrawn anytime. A form of discharge is also sent by the company in order to acknowledge the receipt of the policy amount.

B) Procedure for Settlement of Claim on the Maturity of Insurance Policy

The settlement of maturity claim follows a simple procedure. The procedure gets started soon after the completion of maturity period of a life insurance policy. Prior to the claim settlement, discharge form is sent by the divisional head of the LIC to the policy holder before two months of maturity date. After receiving the filled in discharge form, claim settlement takes place. The procedure of maturity claim settlement include three main steps as follows,

1. Intimation of the Maturity

The first step in the claim settlement is intimation about the maturity to the policy. The divisional officer of the LIC is responsible for intimating the insured about the maturity before two months of maturity date. The insured is asked to fill the discharge form which is sent along with the intimation and submits the required documents. The documents includes the original document of policy, age proof of the insured and the assignment or reassignment deed of the policy. In case where the intimation is not received, the policy holder should approach the concerned branch enquiring about the copy of intimation.

2. Submission of Required Documents

Soon after receiving the intimation letter from the company, the policy holder must forward the following documents to the given address,

i) **Filled up Discharge Form :** Discharge form is issued by the divisional head along with intimation letter. The insured has to duly fill up and sign this letter and forward the same to LIC's branch.

ii) **Original Document of Policy :** Every policy holder is given an original document of the life insurance policy. In case if this document is lost then an indemnity bond with reliable surety needs to be sent.

iii) **Receipts of Premium Paid :** The receipts which acknowledges the payment of premium regularly must be submitted.

iv) **Proof of Age :** Proof of age is also required in settlement of maturity claim. If it is not submitted then it must be sent along with the discharge form. Proof of age can be either a Birth Certificate of insured, High school certificate or any other document given by the authorized body.

v) **Other Documents :** Any other document demanded by the corporation should be submitted.

vi) **Payment of Money :** After successfully receiving the required documents from policy holder, the corporation would send an account payee cheque to the insured. The amount of money would be \according to the terms and conditions of policy selected. The procedure of claim settlement would come to an end after duly paying the claim amount to the insured.

Q3. How to managing claims and losses in insurance?

Ans :

Handling claims is also a social responsibility of insurance company. In case of life the job is not complex as with property liability where losses are have higher frequency, predominance of partial losses and uncertainty of quantum of loss.

Claims management is the basic goal of the insurance industry. It means to settle the losses of the insurer and the differences between the insurer and the insured. Claims management is more than just settling the losses with money. Insurance companies have claim settlement representatives to carry-out this task. An insurance company should pay for the claim reasonably. Rejection of undeserved claims also falls under claims settlement. Claim management is the function of an insurance adjuster. There are various such adjusters working in the insurance industry.

Objectives

The basic objective of claims settlement includes:

1. Confirmation of a Covered Loss

The insurer should make sure that the claim to be covered had actually occurred or not. The insurer should check, if the applicant of a life or property insurance is eligible to claim it.

2. Reasonable and Timely Payment of Claims

The claims settlement should be fair and without any delay. If the applicant's reasonable claim is rejected, it may defy the main objective of insurance. It may also affect the insurer's reputation.

3. Personal Support to the Insured

Apart from the legal responsibilities as per the contract, the insurer should help the insured personally in some cases. **For example,** an insurer should help the insured to find a temporary house, if there is any natural hazard.

Types of Claims Adjustors

The person who adjusts a claim is known as a claims adjustor. The major types of adjustors include the following:

1. Agent

An agent often has authority to settle small first-party claims upto some maximum limit. The insured submits the claim directly to the agent, who has the authority to pay upto some specified amount.

2. Company Adjustor

A company adjustor can settle a claim. The adjustor is usually a salaried employee who represents only one company. After notice of the loss is received, the company adjustor will investigate the claim, determine the amount of loss, and arrange for payment.

3. Independent Adjustor

An independent adjustor can also be used to settle claims. An independent adjustor is a person who offers his or her services to insurance companies and is compensated by a fee. The company may use an independent adjustor in certain geographical areas where the volume of claims is too low to justify a branch office with a staff of full-time adjustor.

4. Adjustment Bureau

An adjustment bureau can be used to settle claim. An adjustment bureau is an organisation for adjusting claims that is supported by insurers that use its services. Claims personnel employed by an adjustment bureau are highly trained individuals who adjust claims on a full-time basis.

5. Public Adjustor

A public adjustor can be involved in settling a claim. A public adjustor, however, represents the insured rather than the insurance company and is paid a fee based on the amount of the claim settlement.

2.2 Underwriting

Q4. Define Underwriting. What are the objectives of Underwriting?

Ans :

Meaning

Underwriting can be termed "assumption of liability". It means signing an insurance policy and thereby becoming liable in the face of a specified loss. Underwriting involves the selection of policyholders after thoroughly evaluating all hazards, establishing prices and then determining the terms and conditions of the insurance policy.

The underwriting framework of a company plays a major role in determining the company's standing in the market. The underwriter must aim to generate profits and minimize losses through a well-balanced underwriting policy. One aspect that the underwriter must always bear in mind is that the underwriting must neither be too strict nor too lenient. If the acceptance criteria are very stringent, then the insurer will miss out on several acceptable businesses and may even face losses because of the expenses involved in cancelling business that the marketing person might have initially agreed to. This can be remedied by including enough conditions to make the risk acceptable. On the other hand, if the acceptance criteria are too liberal, the insurance company may face substantial losses and be forced to withdraw from a given line of business.

Once the risk involved is deemed acceptable, underwriting then fixes the rate of premium, and subsequently, all other terms involved. There are certain guiding objectives and principles that the underwriter must follow.

Objectives

Underwriting has three-fold objectives:

1. Producing a large volume of premium income that is sufficient to maintain and enlarge the insurance company's operations and to achieve a better spread of the risk portfolio;
2. Earning a reasonable amount of profit on insurance operations;
3. Maintaining a profitable book of business (by ensuring underwriting profits) - that contains all the policies that the insurer has in force.

2.2.1 Need for underwriting

Q5. What is the Need for underwriting?

Ans :

Underwriting is the process through which an insurance company decides whether or not to issue the requested insurance and if yes, based upon what terms and conditions. Thus, the concept of underwriting plays a significant role in the private and voluntary insurance markets. It facilitates the insurance organization in the following ways,

1. Helps in Risk Pooling and Fair Pricing

Under any insurance plan, all the insured members contribute to a common money pool. From this money pool amount, the insurance company pays to any insured member who suffers losses against the item insured.

Underwriting helps the insurance firm to objectively and correctly determine the expected loss potential and accordingly arrive at a "Fair Price" which the insurance company should charge to the insured members.

2. Ascertaining Group and Individual Insurance Plans

Underwriting is needed by insurance firms, to create a balanced individual insurance plan and group insurance plan. Incase of group insurance, the whole group is insured, thus underwriting is carried out to ascertain the fair or optimal contribution which need to be made by every group member. Similarly, under the group insurance policy, the insured individual need to contribute insurance premium which should sufficiently cover the expected loss potential.

3. Need in Case of Private Insurance Market

Underwriting plays an important role in case of private insurance markets and not in case of social insurance or made compulsory by the government. This is because in case of government mandated insurance participation every insured member would contribute a fixed amount of premium irrespective of his expected loss potential. For example if government mandated life insurance policy states that every member should contribute rupees 1000 insurance amount a 20 years old employee would contribute the same amount, eventhough the probability of death is more in case of the 65 yeas employee.

2.2.2 Guiding Principles of Underwriting

Q6. What are the guiding principles of underwriting?

Ans :

Insurance is a concept of creation of a fund of premiums collected from various persons by pooling all of their risks, from which the financial losses of those few who suffer from the insured perils are compensated. The theory of probability, which can predict with a certain degree of precision, the possibility of a certain event occurring that can give rise to a claim provided there is sufficient data on past experience, is invariably the basis on which the concept of underwriting rests.

It follows that a prudent underwriter will necessarily have to build up data on claims lodged and this has to be done on a continuous basis. Further this data base has to be separately compiled for each of the different insurance portfolios – Fire, Marine & Miscellaneous. Having put this practice in place, he should follow certain basic principles before accepting a risk.

The principles that guide an underwriter before accepting a risk are:

1. Selecting insureds that fit the company's underwriting

Standards only those insureds whose actual loss experience does not exceed the loss experience assumed in the company's rating structure will be selected. The rate is based on a low loss ratio. For example, if the expected loss ratio is 20 percent and a rate is set accordingly, only those insureds will be selected, who can meet the required criteria, so that the actual loss ratio for the group will not go beyond 20 percent.

2. There should be proper balance within each rate

Classification the underwriter must be able to group insureds in such a way that the average rate in the group is enough to pay for all claims and expenses. Therefore, units with similar loss- producing features are placed in the same class and charged the same rate, ensuring that a below average insured is compensated for by an above average insured.

3. Charging equitable rates

The rates that apply to one group should not be charged to another group as well. This would mean that one group is unduly subsidizing another group. For example, in the case of life insurance, charging the same premium rate for people in the age group of 20-25 years and those in the age group of 50-55 years will result in the younger lot subsidizing the older people. This amounts to overcharging and the younger persons will then look out for some other insurance company that has a more equitable system.

Q7. What are the benefits of underwriting?

Ans :

The benefits of underwriting can be summarized as follows :

(i) Product Equitable to Customer

The underwriter should fairly assess the risk in a personal and fix the premium justifiable to the customer.

(ii) Deliverable to the Customer

Consumers are the final authority for buying the products. If the marketers are not able to sell so that the product becomes undeliverable, the onus is on the underwsriters to carry an introspection of the various factors that caused differences between the consumers and company's expectations.

(iii) Financially Feasible in the Insurance Company

The insurers are not in the business of charity. The underwriting benefit must be reflected by the financial statements. Although, the underwriters are not directly involved in the pricing of insurance products, yet their contribution is an vital as that of actuaries, because they operationalise the business of risk.

Q8. State the applications of underwriting.

Ans :

Several sources of information are available to the underwriter regarding the hazards of a commercial applicant for property and liability insurance:

(a) Application Containing the Insurers Statements

The basic source of underwriting information is the application, which varies for each line of insurance and for each type of coverage. The broader and more liberal the contract, usually more detailed information is required. The questions on the application are designed to give the underwriter the information needed to decide whether to accept the exposure, reject it or ask for additional information.

(b) Information from the Agent or Broker

In some line of non-life insurance, the agent may exercise his underwriting authority. For commercial insurances, the profit-sharing contracts are also entered with the agents, whereby the agent derives a special incentive if the business brought by him has resulted in a profit to the company.

(c) Prior Experiences

The past history of claims is also a source of information. In case of existing clients where the claims experience has been unfavorable, the insurance company penalizes i.e. loads premium for new businesses or renewals of the existing ones.

(d) Inspection

Surveys are also conducted by the company's specialists/consultants to find out the accuracy of information as contained in the proposal form.

2.2.3 Factors affecting Insurability

Q9. What are the Factors affecting Insurability?

(OR)

"Age, Gender, Family, and other affect insurability" - Elucidate.

(OR)

Discuss the Factors affecting Insurability of the insured.

Ans : **(Imp.)**

In deciding whether to issue insurance [selection], and if so, on what terms and conditions and at what price [classification], life insurance companies examine several factors to achieve and ensure that rates should be adequate, equitable and not excessive to insureds for insurance coverage. Life insurance underwriting factors are:

1. Age

Expected future mortality is highly correlated with chronological age. So age is a key factor in determining the rate an individual is to be charged for life insurance. But it is rarely a selection factor. Proof of age is required only at the time of immediate annuity purchase.

2. Gender

Is rarely used as a selection factor, but it is routinely used as classification [rate setting] factor with respect to individual life insurance.

3. Medical aspects

(i) **Physical condition:** The determinants of physical condition are build [includes weight, height and distribution of the weight], nervous, digestive, cardiovascular, respiratory, or genitourinary systems, and glands of internal secretion etc., which reveal an average expected mortality rate.

(ii) **Personal history :** Individual's health record, habits, driving violations, and amount of insurance already owned bear his or her expected mortality.

(iii) **Family history :** Transmission of characteristics by heredity is also important for classification of insureds.

(iv) **Tobacco use :** Using tobacco in any form is an important risk factor by itself, causes expected future mortality to be worse than the average, and is a warrant for separate classification.

(v) **Alcohol and drugs :** Excessive alcohol use is associated with higher than standard mortality.

4. Occupation

The occupation may present environmental hazard [exposure to violence], the physical conditions [persons who work in close, dusty, or poorly ventilated quarters] risk from accident [professional automobile racers, professional divers Because of this, ratings have been reduced or eliminated for many occupations.

2.2.4 Methods of Risk Classification

Q10. What are the methods of risk classification?

Ans :

Risk can be classified through following two methods in Insurance.

1. Judgement or Assessment method

In Judgement or Assessment method, the insurer studies all the features of the life to be insured based on the material information placed before him, draws a mental picture and brings into play all his knowledge and experience to determine terms of acceptance of the risk. The company has to depend upon the combined judgement of those in the medical, actuarial, and other departments who are qualified for this work.

The judgement method functions effectively when there is only one unfavourable factor to consider or where the decision is simply either to accept the application at standard rates or reject it entirely. Where multiple factors are involved or a proper substandard classification needed, this method is not found useful.

It also requires the use of highly skilled personnel for proper risk appraisal. The method also cannot ensure uniformity in the decisions by the same persons at the same or different times. Besides it is a time consuming process.

To overcome the weaknesses of this method, life insurance companies evolved the other method viz., Numerical Rating Method.

2. Numerical Rating method

Under this method, each factor of insurability is compared with medico actuarially prepared standard and deviations are measured in terms of extra debit or credit points. Adverse features attract debit points while favorable ones are given credit points. The sum total of debit ratings of all factors give the extra mortality of a particular life (risk).

Thereafter total extra mortality ratings are matched with standard charts and converted into monetary value which is called the extra premium. It is on the basis of numerical ratings that underwriter classifies the risk and decides the terms of acceptance of risks.

Merits

1. Numerical rating method enables direct usage of the results of various Medico-Actuarial investigations.
2. Numerical rating method reduces the operation of subjective factor in underwriting risks to the minimum.
3. Numerical rating method helps the insurers to evolve a uniform underwriting procedure and classify risk in identical groups.
4. Numerical rating method facilitates building up of new statistics on the basis of which the basic ratings are continuously reviewed in the light of up to date trends in insurance medicine.
5. Numerical rating method ensures that no factor is overlooked.
6. Numerical rating method makes possible uniform assessment either by several underwriters or the same underwriter at different times.
7. Numerical rating method enables business to be handled with greater speed.

Limitations

While the numerical rating method has all the above advantages, it is not without limitations. One of the limitations that it suffers from is that it cannot be extended to assess the occupational hazard and the extra risk resulting from certain standard impairments such as the following:

1. Defects and deformities such as amputated arms and legs, partial or total blindness and deafness, cleft palate, club foot, etc.
2. Standard impairments such as hydrocele, bleeding piles, Caesarean section, etc.

In such cases, the total extra would be obtained by adding the extra premium wherever applicable for the health/physical impairment as per the numerical rating method to the extra premium for occupation and / or other standard impairment if any.

2.2.5 Laws affecting Underwriting

Q11. Discuss in brief the various laws effecting underwriting.

Ans : **(Imp.)**

There are various laws which effect underwriting by the insurance firms. The main aim of these laws is to protect the consumer against fraudulent practices by insurance companies. The important laws affecting underwriting of life and health insurance in the U.S. A are discussed below.

1. FCR Act

The FCR Act (Fair Credit Reporting) Act requires the insurer companies to notify the individual member that he has the right to get the nature and scope of the investigation.

The FCR Act states that,

(i) The insurance company disclose all the consumers information it has collected, along with the source.

(ii) In case of a rejected underwriting decisions, the insurer need to provide detailed reason about the rejection.

(iii) If the consumer is not satisfied with the reason, a reinvestigation need to be carried on free of cost for the consumer.

2. NAIC Act

The National Association of Insurance Commissioners Privacy Protection Act advocates for the protection of the consumer's privacy. The act prohibits the insurance companies against conducting fake interviews for the client to collect information.

3. Unfair Discrimination Laws

This law prevents insurance firms against unfairly charging higher fee, premium or provide lesser benefit to consumers of a specific class. It advocates same rules and regulations for consumers in a same condition.

4. Unfair Gender Discrimination

The U.S supreme court decision in the 1983. Norries case proved that insurance companies can not go for gender base pricing.

5. Unfair Discrimination Based Upon Mental or Physical Health

The law prohibits an insurance companies from refusing or limiting insurance cover for a physically or mentally impaired consumer. Solely based on the improvement.

6. Unfair Discrimination Based on Sexual Preferences

The U.S law prohibits the insurance company against enquiring about a consumer sexual preferences in connection to life insurance or health insurance underwriting.

7. HIPAA

The Health Insurance Probability and Accountability Act (1996) aims to increase access and transferability of health care insurance for the consumers. This is performed through,

(a) Preventing discrimination of the ensured and their family members depending upon the health status.

(b) Limiting about what all can be included and excluded in the preexisting conditions.

2.3 Financial Planning and Taxation: Savings

Q12. Define Financial Planning. What is the role of life insurance policies in financial planning?

(OR)

What is financial planning? Explain the role of life insurance policies in financial planning.

Ans : **(Imp.)**

Financial planning refers the process of determining whether and how an individual can meet life goals through the proper management of financial resources.

Role

Life insurance is a good investment tool which is comparatively simple, affordable and caters to the different stages of the individual's lifecycle. In the present scenario, any one can purchase any kind of insurance policy based on his requirement. However, individuals can adopt a pure protection plan at an early stage which is most affordable or at a later stage which gives the opportunity of earning higher returns. There are various insurance policies which may be related to specific education policies which ensure that your child's education is not compromised in case of an unfortunate situation (death) and there are also some policies related to retirement and pension policies.

It is a fact that insurance is considered as an important element of any sound financial plan. Because there are different types of insurance policies which help to protect one person and his loved ones in different ways. For example protection against accidents, illness, disability and death etc.

The following are the common areas under which a life insurance policy plays a significant role in financial planning,

1. Mortgage Payment

In most cases mortgage is considered as one of the higher expenses like, Payments, taxes, insurance and interest. Because of this reason, large number of individuals plan for long-term financial commitments. However, there will be one question arised from this situation that, if one person get died tomorrow, could his family is able to pay such a huge expenses without your income. In such situation, life insurance policy can help such persons's family by providing a lump sum amount to pay off mortgage debt.

2. Funerals Payments

If one person is having a life insurance policy in his financial plan to cover the funeral cost on his death, then such life insurance policy will support his family to cover up the funeral costs, prevent his family from draining their emergency savings and stopping them to take out a loan at this very difficult time.

3. Educational Payments

If one person is saving very less amount for his child's education while he is alive, but it will be a problem for his child if that person suddenly died. In order to provide some coverage to his children, that person can purchase a life insurance policy which will be a gift of education by factoring educational expenses into your life insurance policy's death benefit. As such, his children can bear the educational cost with benefits of such insurance.

4. Caring for a Special needs Child or Aging Parents

Life insurance policies plays a significant role in a financial plan of person if he have a special child or aged parents that depend on his financial support. Without the resources to provide for their continual care, family members will be forced to take on a stressful and lifelong financial burden. In such situation, life insurance cover can provide the financial support needed for such dependents after the death of that person.

Q13. What do you mean by taxation ? Explain the tax saving through insurance policies.

Ans :

Taxation refers to the practice of a government collecting money from its citizens to pay for public services. In insurance sector taxation is also plays a crucial role because now a days insurance business are on high peaks. Insurance companies are earning higher profits compare to other business companies. Therefore, the taxation of life insurance business in India is currently governed by Section 115 B, Section 44 and the First Schedule of the Income Tax Act, 1961.

Tax Saving Through Insurance Policies

Tax saving or tax-planning is an crucial element of financial planning. If it is planned properly, it will help individuals not only in meeting financial goals but it also help in saving tax from this process. Tax saving for life, health and pension insurance policies are as follows,

1. Tax Savings for Life Insurance Policy

Life insurance policies consist of various policies like, term policies, money back policies, whole life policies, Unit Linked Insurance Plans (ULIPs) and so on. For the purpose of saving tax, all these are treated equally by the Income Tax department. Tax saving can be done by purchasing any of these policies. The premiums paid on these policies can be used for availing tax deduction and hence boost tax saving options.. The following are some details regarding tax deduction on life insurance policies,

The deductions claimed will be added back to income and taxed accordingly if policies are surrendered or terminated before 5 years of commencement. Thus, life insurance plays a major role as a tax saving investment option, by providing various plans which could be the sources of tax saving.

The ICICI Prudential Life Insurance policies provide tax benefits to its applicants in following stages,

Stage 1: Entry Advantage

Individual receive tax benefits on your premium payments under section 80C of Income Tax Act, 1961 (life insurance), 80CCC Income Tax Act, 1961 (pension) and Section 80D Income Tax Act, 1961 (health).

Stage 2: Earnings Advantage

Individual's investment with ICICI will receive the potential to grow and is not currently taxable.

Stage 3: Exclusive Switching Advantage

Individual can switch between equity, debt and balanced funds anytime and these switches are not taxable.

Stage 4: Exit Advantage

Individual receive a tax free Maturity Benefit (the payout you receive when your policy ends) subject to conditions of Section 10 or 1OD of the Income Tax Act, 1961.

2. Tax Savings for Health Insurance Policy

Health insurance policy also offers tax benefits to individuals. It offers Insurance premium up to ` 20,000 for senior citizens and ` 15,000 for others which is eligible for tax benefit. For example, if an individual pays ` 15,000 as premium on his own policy and ` 20,000 for his parent(senior citizen) he can claim tax benefit of ` 35,000 (` 15,000 + 20,000). Therefore, it is considered as efficient tax saving investment plan for a individual.

3. Tax Savings for Pension Policy

Pension plans or annuity plans are another form of life insurance with a different end objective. While life insurance is used to protect the family of a individual after his death, pension is designed to provide benefits for the individual and his family even when he alives. It is also a best plan for tax saving for individual's income.

2.3.1 Insurance vis-a-vis-Investment in the Units Mutual Funds, Capital Markets

Q14. What is mutual fund? What are the types, advantages and disadvantages of Mutual funds.

Ans :

Mutual Fund is a type of collective investment method by which many people pool their money in a fund and invest in various securities like stock, bonds or cash investments. Every mutual fund has a fund manager or investment advisor so it is also called as managed funds. In world's top stock markets collective investments holds a major share because of its flexibility. Depends on the objective of the funds like long term growth and low risk factor or high income growth with high risk factor or low growth rate and stability of principal, fund manager invests in respective fields on behalf of shareholders. For individual investors it is very easy type of investment because someone else manages their funds, take care of accounts and invest money over many different available securities.

Types

Mutual fund schemes may be classified on the basis of its structure and its investment objective.

1. By Structure

(a) Open-ended Funds

An open-end fund is one that is available for subscription all through the year. These do not have a fixed maturity. Investors can conveniently buy and sell units at Net Asset Value ("NAV") related prices. The key feature of open-end schemes is liquidity.

(b) Closed-ended Funds

A closed-end fund has a stipulated maturity period which generally ranging from 3 to 15 years. The fund is open for subscription only during a specified period. Investors can invest in the scheme at the time of the initial public issue and thereafter they can buy or sell the units of the scheme on the stock exchanges where they are listed. In order to provide an exit route to the investors, some close-ended funds give an option of selling back the units to the Mutual Fund through periodic repurchase at NAV related prices. SEBI Regulations stipulate that at least one of the two exit routes is provided to the investor.

(c) Interval Funds

Interval funds combine the features of open-ended and close-ended schemes. They are open for sale or redemption during pre-determined intervals at NAV related prices.

2. By Investment Objective

(a) Growth Funds

The aim of growth funds is to provide capital appreciation over the medium to long- term. Such schemes normally invest a majority of their corpus in equities. It has been proven that returns from stocks, have outperformed most other kind of investments held over the long term. Growth schemes are ideal for investors having a long-term outlook seeking growth over a period of time.

(b) Income Funds

The aim of income funds is to provide regular and steady income to investors. Such schemes generally invest in fixed income securities such as bonds, corporate debentures and Government securities. Income Funds are ideal for capital stability and regular income.

(c) Balanced Funds

The aim of balanced funds is to provide both growth and regular income. Such schemes periodically distribute a part of their earning and invest both in equities and fixed income securities in the proportion indicated in their offer documents. In a rising stock market, the NAV of these schemes may not normally keep pace, or fall equally when the market falls. These are ideal for investors looking for a combination of income and moderate growth.

(d) Money Market Funds

The aim of money market funds is to provide easy liquidity, preservation of capital and moderate income. These schemes generally invest in safer short-term instruments such as treasury bills, certificates of deposit, commercial paper and inter-bank call money. Returns on these schemes may fluctuate depending upon the interest rates prevailing in the market. These are ideal for Corporate and individual investors as a means to park their surplus funds for short periods.

(e) Load Funds

A Load Fund is one that charges a commission for entry or exit. That is, each time you buy or sell units in the fund, a commission will be payable. Typically entry and exit loads range from 1% to 2%. It could be worth paying the load, if the fund has a good performance history.

(f) No-Load Funds

A No-Load Fund is one that does not charge a commission for entry or exit. That is, no commission is payable on purchase or sale of units in the fund. The advantage of a no load fund is that the entire corpus is put to work.

3. Other Schemes

Tax Saving Schemes : These schemes offer tax rebates to the investors under specific provisions of the Indian Income Tax laws as the Government offers tax incentives for investment in specified avenues. Investments made in Equity Linked Savings Schemes (ELSS) and Pension Schemes are allowed as deduction u/s 88 of the Income Tax Act, 1961. The Act also provides opportunities to investors to save capital gains u/s 54EA and 54EB by investing in Mutual Funds.

Advantages

1. Flexibility

The investments pertaining to the Mutual Fund offers the public a lot of flexibility by means of dividend reinvestment, systematic investment plans and systematic withdrawal plans.

2. Affordability

The Mutual funds are available in units. Hence they are highly affordable and due to the very large principal sum, even the small investors are benefited by the investment scheme.

3. Liquidity

In case of Open Ended Mutual Fund schemes, the investors have the option of redeeming or withdrawing money at any point of time at the current rate of net value asset.

4. Diversification

The risk pertaining to the Mutual Funds is quite low as the total investment is distributed in several industries and different stocks.

5. **Professional Management**

The Mutual Funds are professionally managed. The experienced Fund Managers pertaining to the Mutual Funds examine all options based on research and experience.

6. **Potential of Return**

The Fund Managers of the Mutual Funds gather data from leading economists and financial analysts. So they are in a better position to analyze the scopes of lucrative return from the investments.

7. **Low Costs**

The fees pertaining to the custodial, brokerage, and others is very low.

8. **Regulated for Investor Protection**

The Mutual Funds sector is regulated by the Securities Exchange Board of India (SEBI) to safeguard the rights of the investor.

Disadvantages

1. **Dilution**

Even though diversification reduces investment risk it dilutes returns. A mutual fund is a portfolio of number of assets. So the returns of a fund are the average return of securities in the portfolio.

2. **Management Fees**

Some part of our investment (usually 1% to 2% annually) goes towards the management fees. Apart from this there are sales commissions and redemption fees.

Note: As per the recent SEBI directive entry load is waived off even if our buy order goes through a dealer/broker.

3. **No Guaranteed Returns**

Returns from mutual fund investments are not guaranteed though they are managed by professionals. Most of the mutual funds don't beat their benchmarks.

4. **No Control Over Decisions**

We don't have any control over the investment decisions. The manager takes all decisions on securities buying and selling.

5. **Regulations**

Though strict regulations are to ensure safety of investor's money they don't allow free trading which may result in less returns. I will try to cover SEBI general rules on mutual funds in coming posts.

6. **Inefficiency of Cash Reserves**

Mutual funds maintain huge cash reserves to meet redemptions at same time. These cash reserves could be a combination of cash in bank, cash equivalent highly liquid money market instruments. So some part of the money is inefficient which could have been invested to get more returns.

7. **Taxes**

If the money you invest in Mutual Fund earns a profit, you will be required to pay the taxes on the dividend received by you. You have to pay the taxes even if you make your money reinvest in Mutual Fund.

Q15. Explain the how insurance and mutual funds related.

Ans :

The concept of mutual fund is used in building Unit Linked Insurance Policy (ULIP) which is type of life insurance policy. However, the structure and working pattern of ULIP is different from mutual funds. Most of the insurance companies try to position their products as mutual funds in the market but it is very difficult for insurance products to deliver those benefits as provided by mutual funds. In mutual funds, the investment amount is decided by the fund houses and under ULIPs. The premium contribution is decided by the policy holder and also it varies based on the term of policy.

ULIPs provided dual benefits i.e., one side it provide insurance cover and on other side it allow to earn return through investment. Thus, insurance companies also floats funds like mutual funds institutions in order to gather investors. Insurance companies invest this money in assets like stock and bonds due to which it sounds like a mutual funds because of such investment.

The major difference between ULIPs and mutual fund is that ULIPs provide life coverage which a mutual fund does not provide to the investors. However, the common thing which is there between these two investments that both are exposed investors to market risks and maintain professional fund managers to manage the assets of investors.

Following table show the differences between ULIP's and mutual funds,

S.No.	Basis	Mutual Fund	ULIPs
1.	**Nature**	It is a investment.	It is a investment and insurance cover.
2.	**Tax**	For this, only Equity Linked Saving Schemes (ELSS) gives tax deductions.	For this, tax is charged as section 80c of income tax Act, 1961.
3.	**Lock Period**	One can withdraw funds within 1 year only 1% fund value will be deducted for early withdrawals.	Minimum lock period is 5 years. No one can with -draw before this period,
4.	**Fund Charges**	Fund charges will be 2.5% on this.	Fund charges will be 1.35% on this.

Q16. Explain the concept of investment of insurance companies in capital market.

Ans :

Capital market is a market under which money is provided for periods longer than a year. Most of the insurance companies invest their money in capital markets which they collected through premiums and income from investments. They invest major part of their funds in government, semi-government and government approved securities followed by industrial securities. During the period 1990-2016, the investment in industrial securities has increased from 10- 25% respectively.

Most of the capital market deals for insurance companies are still basically financial driven. However, in order to strengthen their capital position, companies can raise equity or debt. The insurance sector of India is capable of raising substantial amounts of equity in the market.

Recently, insurance companies started using risk securitization techniques for transferring insurance risk to the capital markets. In addition, the capital markets will have the potential to help the insurance market by providing additional capacity which is above the limit provided by re-insurance market.

The various insurance companies which are investing in capital market are as follows,

1. Life Insurance of India (LIC)

LIC is one the largest life insurance company in India which has total assets of ` 23 trillion. The LIC has highest number of policyholders and the largest premium based the state-run insurer grew faster than the industry in terms of first year premiums in financial year 2016-17.

According to Insurance Regulatory and Development Authority of India (IRDA) during financial year 2016- 17, the life insurance industry of India total income from first premium increased to ` 1.75 trillion. During 2017, the LIC's first year premium collection was ` 1.24 trillion which contributes 71% of total industry collection.

2. SBI Life Insurance

SBI Life Insurance hitted the capital market on September 2017 by ` 8,400 crores. The reported profit of SBI during financial year 2016-17 was ` 954.65 crores.

2.3.2 Life Insurance in Individual Financial Planning

Q17. Explain the process of life insurance in individual financial planning?

Ans :

While selecting a life insurance plan, every individual need to verify its financial position because based on his financial capability only he can pay the premiums of life insurance policies. As such individual financial planning becomes necessary in life insurance.

Individual financial planning is the process of managing individual's money to achieve financial objectives of him and his family. However, inorder to achieve financial objectives successfully, a systematic financial planning is required which fits the life insurance policies. This process consists of six steps, which are as follows,

Step-1: Collection of Information

In this step qualitative and quantitative information is collected. For example, information may be related to individuals assets, liabilities, income and expenditure, investment, life styles, economic position, family background etc.

Step-2: Establishment of Objectives

The 2nd step is most crucial in the process of individual financial planning process because in this step the objectives of the process will be established. These objectives are categorized into short-term and long-term objectives which may cover living standards of the family, quality eduction for the children, health security, retirement benefits etc.

Step-3: Information Analysis

In this step, the information which is collected from individual like qualitative and quantitative information will be analyzed.

Step-4: Development of Plan

In this step, an effective plan is developed with the help of gathered information (Step-1), objectives which is established (Step-2) and analyzed information (Step-3).

Step-5: Implementation of Plan

In this step, an effectively developed plan is implemented.

Step-6: Monitoring and Reviewing of Plan

This is the last step in the. process of individual financial planning. In this step the information is monitored and reviewed in a sophisticated manner.

2.3.3 Implications in IT treatment

Q18. Explain the implication of income tax of life insurance companies.

Ans :

The taxation of Indian life insurance companies is regulated and governed by sections 115B, section 44 and first schedule of Income tax Act, 1961.

The section 115B of Income Tax Act, 1961 states that,

1. The income tax shall be aggregate of amount generated from the total income of assessee which consist of any profits and gains from the business.
2. The income tax amount shall be calculated at the rate of 12.5% on the profits and gains of life insurance business which consist of total income.

After this statements, two changes has been brought up. In one, the rate of tax will be 12.5% on calculated profit and gains of life insurance business and other one is normal corporate tax rate on the net income on the funds of shareholders after excluding the profits from life insurance business.

According to Section 80D of Income Tax Act, 1961, Section 10(1OD) says that any moneys received under a life insurance policy will not constitute 'income' under the Income Tax Act chargeable to Tax in the year of receipt. There is no limit of payment of

(i) Refund of premiums

(ii) Surrender value

(iii) Loans

(iv) Survival benefit

(v) Maturity claim

(vi) Death claim, etc.

These amounts need not be shown as income in the tax returns filed. But the premiums paid under section 80 DD, if refunded, are treated as income chargeable to tax.

Taxation on Insurance Premium

The maturity proceeds from the single premium life insurance policy will be tax-free only if the minimum sum assured throughout the policy term remains at least 10 times of the single premium paid. However, if the sum assured on single premium life insurance policies is 1.25 times of the premium amount, then the maturity proceeds will be taxable. For example: when the premium is ` 10,000, the life cover (sum assured) should be ` 1 00,000 for the maturity proceeds to be tax-free. If, say, the sum assured is ` 12,500 or ` 90,000, the policy loses the tax benefit under Section 10 (10D). Therefore, make sure the sum assured is at least 10 times the premium amount.

If this condition is not satisfied then the complete maturity which is proceeds fully taxable in the year of receipt. It has to be shown as income while filing income tax return. The only exception in this case is the proceeds from life insurance policy arising due to the death of the policyholder are exempt from tax irrespective of the level of the premium.

Addition to this, the insurer is supposed to deduct tax at source i.e. TDS on such payments. According to section 194DA of the Income Tax Act, 1961, any sum received by an insured or Indian resident from an insurer under a life insurance policy shall be subject to TDS of 1 percent if the maturity proceed is not exempted under Section 10(10D), i.e., on policies where the sum assured is less than 10 times the premium amount.

Taxation on Annuity or Pension Plans (Sec. 80CCC)

According to Section 80CCC of Income Tax Act, 1961, contributions-made towards annuity plans available with any of the Life Insurance Companies for receiving pension from the fund can be considered for tax benefit. The maximum Tax deduction allowed under this section is ` 1.5 Lakhs.

Taxation on Medical Insurance Premium (Sec. 80D)

According to Section 80D of Income Tax Act, 1961, upto ` 30,000 can be deducted towards the medical insurance premium for senior citizens (above 60 years) and upto ` 25,000 can be deducted towards medical insurance of self and dependents (spouse & children).

Additionally, a deduction of up to ` 25,000 towards medical insurance premium of parents (father/mother/both) is available. If both the parents (Father & Mother) are senior citizens, then the deduction allowed is up to ` 30,000.

2.4 GENERAL INSURANCE - CONCEPT OF UNDERWRITING

Q19. Explain the concept of under writing.

Ans :

Underwriting is a critically important function and is performed each time an insurance application is taken. Its purpose is to determine if applications represent risks acceptable to the insurer to determine whether or not the insurer will issue a policy to an applicant. Underwriting is based on a variety of criteria, established by each insurer and regulated by state and federal law. Each underwriting decision involves balancing the insurer's desire to earn premium with the insurer's ability to cover claims and remain in compliance with regulatory financial requirements while making a profit.

Underwriting is the function of evaluating the subject of insurance, whether a person, property, profession, business, or other entity, and determining whether to insure it. The underwriter must apply company standards to each applicant, and, based on these standards, ascertain whether the application represents an acceptable risk. Underwriting is the foundation of the insurance transaction process.

The term underwriter arose out of marine insurance. In the 17th Century, merchants who were willing to take on a portion of the risk for voyages would list the amount of the voyage they were willing to insure and sign their names underneath a contract that detailed the terms of the risk.

These merchants became known as underwriters because they wrote their names under the contract terms. Since that time, the insurance business has evolved and policies are no longer underwritten by individuals who insure risks, but the term underwriter continues to be applied to those who review and select risks to insure.

SEBI's Guidelines for Underwriting

According to SEBI, the number of underwriters should be decided well in advance by the issuer and he must obtain prior permission from SEBI. Permission will be granted by SEBI only after finding out the net worth of the underwriters and their outstanding commitments.

The Stock Exchange, where the security is going to be listed must also be informed about the arrangements made with the underwriters.

25% of each class of securities must be offered to the public and in the remaining 75%, the following method of firm allotment could be adopted.

SEBI has instructed companies to allot to three major categories of allotees, namely,

1. QIB
2. HNI
3. Retailers

1. **QIB :** refers to qualified institutional bidders (Mutual Funds, banks, etc.).
2. **HNI :** refers to high net worth individuals, investing more than Rs. 1 lakh in a single company security.
3. **Retailers :** are individuals who are investing less than Rs. one lakh.

Q20. Explain the Need and Significance of Underwriting.

Ans :

Whenever new issues of capital are made, there is always certain risk of non-subscription or under- subscription of securities by the public. The plans of the promoters of the companies remain unimplemented and their reputation adversely affected if the issues are not successful.

Underwriting is a safer way of marketing securities for new issues of capital. It is an insurance in the sense that it provides protection against such risks.

Thus, it is a very useful method of raising finance through issue of securities (shares and debentures). It is not only the issues of equity share capital that need be underwritten. The analysis of underwriting of issues indicates that almost 100 percent of the issues of preference share capital and debentures are underwritten in India.

Although, the need for underwriting of initial issues is more, especially in case of new unexperienced promoters; the further issues of capital are also underwritten. The extent of underwriting required depends upon the nature of the project, the state of the capital market, the general response of the investors and the reputation of the promoters.

Thus, underwriting plays a very significant role in corporate financing.

The importance of underwriting can further be highlighted from the following functions performed by the underwriters :

1. Assurance of Adequate Finance

Underwriting is an act of undertaking guarantee by an underwriter to buy and pay for the shares or debentures placed before the public in the event of their non-subscription. Thus, through underwriting, an issuing company is assured of procuring the required funds from the issue of shares or debentures.

In the event of non-subscription by the public, underwriters purchase the unsubscribed part of the issue and provide finance to the company.

2. Supplying Valuable Information to Companies

In addition to the protection of risk of the issuing companies with regard to the success of the issue, the underwriters supply valuable information in regard to capital market conditions, general response of the investors, etc. to the issuing companies. These companies are, usually, benefited from the expert-advice of the underwriters.

3. Distribution of Securities

After purchasing securities, underwriters distribute the same to the real investors. The underwriters, through agents and others diffuse the issue over a large number of investors scattered in different part of the country. Thus, underwriting helps promoters to retain control over the management of the company.

4. Increase in Goodwill of the Issuing Company

The underwriting of capital issues by prestigious institutions generates confidence among investors and improves their response to the issues. Investors in advanced countries are influenced more by the prestige of the underwriting agencies than by the prestige of the issuing company. Underwriting, thus, ultimately increases the goodwill of the issuing company.

5. Service to Prospective Investors

Underwriters provide essential information about the issuing companies to the prospective investors and also advise them about various issues. They encourage people to save more and direct their savings in corporate securities. Thus, investors are also benefited through underwriting.

6. Service to the Society

The pace of industrialisation of a country depends to a great extent upon the successful flotation of capital issues. By mobilising resources and providing adequate finance, underwriters play a very important role in setting up of new projects, increasing employment, production and per capita income. Thus, it is not only the corporate enterprises but also the society at large which is benefited by underwriting.

Q21. State the various types of underwriting.

Ans :

The various types of underwriting are as follows:

1. Syndicate Underwriting

Syndicate underwriting is one in which, two or more agencies or underwriters jointly underwrite an issue of securities. Such an arrangement is entered into when the total issue is beyond the resources of one underwriter or when he does not want to block up large amount of funds in one issue.

2. Sub-Underwriting

Sub-underwriting is one in which an underwriter gets a part of the issue further underwritten by another agency. This is done to diffuse the risk involved in underwriting. The name of every under-writer is mentioned in the prospectus along with the amount of securities underwritten by him.

3. Firm Underwriting

Firm underwriting is one in which the underwriters apply for a block of securities. Under it, the underwriters agree to take up and pay for this block of securities as ordinary subscribers in addition to their commitment as underwriters. The underwriter need not take up the whole of the securities underwritten by him. For example, if the underwriter has underwritten the entire issue of 5 lakh shares offered by a company and has in addition applied for 1 lakh shares for firm allotment. If the public subscribes to the entire issue, the underwriter would be allotted 1 lakh shares even though he is not required to take up any of the shares.

Q22. State the various Principles of Underwriting.

Ans :

Underwriting is the most important element of any insurance plan. Therefore, the insurance firm need to be careful while dealing with the underwriting of the different insurance policies. These policies need to be drafter in a manner which are not just fair but also socially and legally acceptable.

The insurance companies may follow the below mentioned guiding principles in underwriting.

1. Big Standard Group

An important guiding principle in under-writing is that the insured group need to be large. This would ensure that the group is stable, has a good quantity of funds, posses predictable mortality and the overall average cost would be reduced. This is the reason why 90% of the insurance applications are accepted by the insurance firms.

2. Optimal Group Balancing

The insurance company need to strike a balance between the size of the substandard group and the insurance premium to be charge. Further, the insurance firm need to ensure that it does not loose its competitive advantage in the market. For example if there are a large number of insured who are smokers, the insurance firm may find the group into smokers and non-smokers and charge a premium accordingly.

3. Intra Group Balancing

An important principle of underwriting is that the insurance company need to balance the group from within I.e., there should be a good mixture of insured individual comprising of members whose loss experience is higher and also members whose loss experience is lower. This would ensure that the group is balanced. Further based upon the probable risk factor, the insured may be charged differential insurance premium.

4. Socially Acceptable Guidelines

The insurance underwriting principles need to be socially acceptable. Generally insurance firms charge individuals according to the risk they reflect i.e., an individual with a high probability of experiencing loss would be charged more and vice versa.

However, a research study conducted in the U.S.A and found that 49% of the respon-dends believe it is 'ok' to charge more to old insured members with more risk of dying early. However, 39% of the survey respondends fell that it is unfair to charge more to retired, risk and old members.

In the united states, insurance companies, used to charge more to African Americans members compared to white Americans stating that the lifestyle of African, American make them more risky group. However, most people felt that it is unfair to charge more to someone, based upon their race.

Thus, it may be concluded that the insurance firms need to make their underwriting rules objectives, fair, socially and legally acceptable, to remain competitive and successful in the insurance industry.

2.4.1 Underwriting Process

Q23. What are the steps involved in under-writing process ?

Ans :

The steps involved in underwriting are as follows,

Step-1: Classification of Applicants

The applicants are classified into different categories based on the risks associated and the rate of premium.

(a) Standards Risks : The applicants under this category perform according to the standards of insurance company the premium does not include any surcharges.

(b) Preferred Risk : The applicants whose loss experience is above average and below the company standards are included under this category.

Example: Non-smokers.

(c) Sub-standard Risk : The applicants whose loss experience is below average are included in this category. These policies are called rated or extra risk policies. The premium rates are high in this category.

(d) Uninsurable Policy : The applicants under this category are not qualified for insurance.

Example: Persons with uncurable/rare disease, high moral hazards etc.

Step-2: Agent as First Underwriter

Agent should be made aware of the criteria for eligibility of the applicants as insureds. In case of auto insurance an agent should not accept the applicants from drunkers, single drive before the age of 21 years and drivers of high powerful sports car.

In case of property and casualty insurance, agent can directly bind with the insurer immediately related to the disapproval and cancellation of the application. Agents should be paid a premium and also compensation for the losses in the process of underwriter.

In case of life insurance, agent should follow the criteria to select the applications that is mentioned under the underwriting policy of a company. The applicants who are drug adictors, alcoholics and workers in hazardous occupations etc., should not be approved as insureds.

Step-3: Sources of Information

The different types of information regarding the applicants is necessary for an underwriter whether to accept or reject their applications. The information differ with the type of insurance.

In case of property insurance underwriter should consider the personal characteristics of the applicant including the presence of moral hazard, financial condition etc. Physical features of the property such as type of construction, quality of the building and other aspects of the property. They also require the financial position of the applicant and past loss experience, living habits and moral characteristics of applicant.

An underwriter can obtain information from different sources such as,

i) Application

ii) Agent report

iii) Inspection report

iv) Physical inspection

v) Physical examination

vi) MIB report.

(i) Application : It forms basic source of information for underwriters. Information in an application varies from one insurance company to other. In case of life insurance an application will furnish the information related to the age, gender, weight, occupation, personal and family, health and hazard habits of the applicants.

(ii) Agent Report : Underwriter can also obtain information related to applicants from the evaluation report submitted by agents. In case of life insurance an agent will assess the applicant's information by estimating the annual income, plans of the applicants related to life insurance etc.

(iii) Inspection Report : An underwriter can also obtain proper information regarding the applicant from the outside firms in the form an inspection report. Through which an underwriter can estimate the moral hazards. In case of life insurance the inspection report provide the information about the current financial condition of the applicant, the debts, delinquent bills, policy accord, felony convictions and other additional information that depicts the credit worthiness of the applicants.

(iv) Physical Inspection : In case of property and liability insurance underwriter should obtain information related to the property of the applicant through physical inspection. Through this an agent or any representative of insurance company have to inspect the property and should submit the report to the underwriter. In case of workers compensation insurance, the information in a physical inspection report include the unsafe working conditions include the damaged machines, violation of safety rules etc.

(v) Physical Examination : Physical examination of the applicant is also very important in case of life insurance company. An underwriter can obtain information related to weight, body condition of the applicant. This report should be provided by the approved physician only.

(vi) MIB Report : MIB report also constitute one of the source of information for an underwriter. This report consists of information about the health impairments of the applicant such as high blood pressure, heart problems, etc.

Step-4: Underwriting Decisions

Based on the information furnished from the above sources help an insurer in taking appropriate decisions. The three important decision of an underwriter include,

(a) First decision is acceptance of application for issuing the policy.

(b) Second decision is to accept the application according to the restrictions as per the company's underwriting policy. In case of crime, insurance policy the applicant should satisfy the requirements that are necessary to issue the policy such as maintenance of burglar alarm system.

(c) Third decision is to reject the application. The inappropriate decision regarding the rejection of application will reduce the revenues of the insurer and agents.

Most of the insurance companies are using computerised underwriting services in case of standard life insurance type.

Example : Auto insurance and home owner insurance policy.

Step-5: Other Considerations

The factors that should be considered in the process of underwriting include the interrelationship of underwriting activities with the other functions of insurer such as rate adequacy, reinsurance and renewal of policy.

(a) Rate Adequacy and Underwriting : The rates have significant effect on underwriting profits and losses. If the rates determined by the insurer are adequate for a class they can expand the underwriting for new business, otherwise they require conservative approach for new business. Insurer will terminate the business activities if the insurance policies involve high moral hazards.

- In case of commercial property and casualty insurance, the underwriting activities have a significant effect on the price of the policy. It is also associated with commercial risks in the price negotiations between the line underwriters and agents.

- In commercial liability and multiplier insurance underwriting activities are not subject to more restrictions and also generate more profits if the rates are acceptable and adequate. Insurer will incur underwriting losses if the restrictions are more.

(b) Reinsurance : The presence of reinsurance option may reduce the restrictions of the underwriting policy of insurer.

(c) Renewal : Life insurance policies cannot be cancelled whereas property and liability insurance policies are cancellable but not renewed. The insurer have a right to cancel the policy in case of fraudulent actions but some states have imposed some restrictions on the right of insurer to cancel the policy.

2.5 Risk Sharing and its Methods

Q24. Define risk sharing. Explain the various elements and methods of risk sharing.

Ans : **(Imp.)**

Meaning

Risk sharing means that the premiums and losses of each member of a group of policyholders are allocated within the group based on a predetermined formula. Risk is considered to be shared if there is no policyholder-specific correlation between premiums paid into a captive, for example, and losses paid from the captive's reserve pool. Risk sharing is the practice of distributing risks amongst organizations, departments, teams or individuals.

Sharing risk is often implemented through employer-based benefits that allow for the company to pay a portion of insurance premiums with the employee. Larger companies with more employees can negotiate even lower fees, due to the economies of scale that they bring to the table. In essence, this shares the risk with the company and all employees participating in the insurance benefits. Sharing is a method to drive down costs in order to minimize retention risk. Individuals may find it in their best interest to partake in sharing the risk with matching employer health care and life insurance plans.

This concept is a structural theme behind the state health insurance exchanges mandated by "Obama care." The understanding is that with more participants sharing the risks, the costs of premiums should shrink proportionately. Whether the intended objective is reached is up for debate, as health insurance premiums continue to rise annually. From the health insurance company's perspective, the premiums from healthy members should offset the expenses for the ailing members. In the past, insurance companies could mitigate some of the risk during the enrollment process by limiting or denying coverage to individuals with pre-existing medical conditions.

By refusing to cover individuals associated with the higher medical costs, insurers were able to better manage costs. The exception was within group plans. Since Obama care was signed into law in 2010, with major implementation roll-outs in 2014, insurers can no longer deny coverage based on pre-existing conditions or health reasons, with the exception of short-term health insurance. This has resulted in sky-rocketing costs that can only be mitigated by raising premiums across the board for all members.

Elements

It has several common elements :

1. Insurance

Insurance products designed to pool risks amongst clients.

2. Self-Insurance

Self-insurance is a pooling of risks within an organization to reduce the maximum impact to any one team or department.

3. Mitigation

Risk sharing may provide opportunities for an organization to mitigate risks. For example, resource risks shared between multiple teams may provide opportunities to share resources and reduce risk.

4. Commitment

Risk sharing may be used as a strategy to improve the commitment of stakeholders to a project. For example, if operations and marketing share the risks of a project it may be more likely to succeed versus a situation whereby operations bear all risk.

Methods

Various Risk sharing methods are given bellow:

1. Risk Avoidance

Avoidance is the elimination of risk. You can avoid the risk of a loss in the stock market by not buying or shorting stocks; the risk of a venereal disease can be avoided by not having sex, or the risk of divorce, by not marrying; the risk of having car trouble, by not having a car. Many manufacturers avoid legal risk by not manufacturing particular products.

Of course, not all risks can be avoided. Notable in this category is the risk of death. But even where it can be avoided, it is often not desirable. By avoiding risk, you may be avoiding many pleasures of life, or the potential profits that result from taking risks. Those who minimize risks by avoiding activities are usually bored with their life and don't make much money. Virtually any activity involves some risk. Where avoidance is not possible or desirable, loss control is the next best thing.

Ways of Risks Avoidance

There are two ways of avoiding risk. They are as follows,

(a) Risk Transfer: Transferring of risk plays an important role in the financial system. Selling off an asset that act as a source of risk is one of the basic method of transferring risk. Example: Consider a car owner is subjected to two types of risk damage due to accident, reduction in its value or damage due to natural calamities. Therefore, by selling the car he can get rid of all the risks.

(b) **Risk Aversion:** Risk aversion refers to the technique in which the investor choose one project which is less risker from the other investment projects. If two investment projects have similar cost and expected return is also same, but the return from one of the project is less certain and the return from the other project is more certain, then the project containing high certainty will be selected.

2. Loss Control

Loss control can either be affected through loss prevention, which is reducing the probability of risk, or loss reduction, which minimizes the loss.

Loss prevention requires identifying the factors that increase the likelihood of a loss, then either eliminating the factors or minimizing their effect. For instance, speeding and driving drunk greatly increase auto accidents. Not driving after drinking alcohol is a method of loss prevention that reduces the probability of an accident. Driving slower is an example of both loss prevention and loss reduction, since it both reduces the probability of an accident and, if an accident does occur, it reduces the magnitude of the losses, since accidents at slower speeds generally cause less damage.

Most businesses actively control losses because it is a cost-effective way to prevent losses from accidents and damage to property, and generally becomes more effective the longer the business has been operating, since it can learn from its mistakes.

Types of Loss Control

The following are the different types of loss control methods,

(a) **Severity Reduction :** This technique focuses on the reduction of severity of the losses. Example: A car manufacturing company installs air bags in its cars. This does not result in reduction in the number of accidents but reduces the injuries caused due to accidents.

(b) **Separation :** This loss control method focuses on reducing the amount of loss associated with specific risks.

(c) **Duplication :** In this technique, the duplicate equipments are made ready to replace the damaged items or equipments immediately.

Timing

(a) **Pre-Loss Activities :** Such loss control activities are implemented before the occurrence of losses.

(b) **Concurrent Loss Control :** When the activities take place in concurrent with the losses, then it is known as concurrent loss control timing.

(c) **Post-Loss Activities :** The timing of loss control activities is known as post-loss when it focuses on the severity reduction.

Decisions in Relation to Loss Control

The loss control is one of the major issue for the risk managers. The cost being incurred on the loss control is one of the major factor to be considered when taking decision with respect to loss control. The loss control method that involves huge cost should be avoided.

Basically, the loss control method is selected on the basis of income or gain expected from an investment. If the expected gain equals the expected costs then the investment in loss control method can be made.

3. Risk Retention

Risk retention, (aka active retention, risk assumption), is handling the unavoidable or unavoided risk internally, either because insurance cannot be purchased or it is too expensive for the risk, or because it is much more cost-effective to handle the risk internally. Usually, retained risks occur with greater frequency, but have a lower severity. An insurance deductible is a common example of risk retention to save money, since a deductible is a limited risk that can save money on insurance premiums for larger risks. Businesses actively retain many risks what is commonly called self-insurance because of the cost or unavailability of commercial insurance.

Passive risk retention is retaining risk because the risk is unknown or because the risk taker either does not know the risk or considers it a lesser risk than it actually is.

Types

The following are the different types of retentions,

(a) Planned Retention : Planned retention is the retention under which the risk is recognized. Plans and conscious efforts are made for the assumption of recognized risk. Most organizations prefer planned retention as it is the most convenient technique for risk management. Absence of alternatives also forces the organizations to adapt planned retention.

(b) Unplanned Retention : Unplanned retention refers to the retention made by a firm without the recognition of exact risk. If the organization under estimates the possible loss associated with the risk, an unplanned retention type is believed to be adopted by the organization.

(c) Unfunded Retention : Unfunded retention refers to the retention where no funds are arranged in advance for the payment of losses.

(d) Funded Retention : When the organization makes an arrangement of funds in advance to pay for the losses that may occur in the future, it is said to follow a funded retention type. Funded retention may be in any of the following type,

(i) Credit : A credit line may be drawn up by the manager to fund the losses that arise as a result of retained risks. There is no proper source for payment of huge losses unless the credit line is decided by the manager.

(ii) Reserve Funds : A firm may establish a reserve fund to pay off losses arising from the risks retained by the firm. In case of huge losses, reserve funds may prove to be ineffective.

(iii) Self-Insurance : A self-insurance may also be used to fund the risk of the firm. This is possible when firm has large units that have the ability to predict losses. An organization can re-fund the expected losses by introducing special funds for the required purpose. Self-insurance does not involve transfer of risk.

(iv) Captive Insurers : Under this method, organizations bring together risk retention and risk transfer. The risk is retained by the firm and the payment for losses is made by the insurers.

Elements to be considered while deciding on retention

The following elements should be taken into consideration while deciding the retention levels,

(a) The organization should take into consideration the total assets, revenues, liquidity of assets, cash flows, working capital, ratio of revenues to net worth, retained earnings and ratio of total debt to net worth.

(b) The firm's ability to predict losses should also be taken into consideration. The firm must be able to predict the accurate range of possible losses.

(c) The feasibility of the retention program should also be taken into consideration. The administrative expenses associated with several losses overtime should be also be considered.

4. Non-insurance Transfers

Risk can also be managed by noninsurance transfers of risk. The 3 major forms of noninsurance risk transfer are by contract, hedging, and, for business risks, by incorpora-ting. A common way to transfer risk by contract is by purchasing the warranty extension that many retailers sell for the items that they sell. The warranty itself transfers the risk of manufacturing defects from the buyer to the manufacturer. Transfers of risk through contract is often accomplished or prevented by a hold- harmless clause, which may limit liability for the party to which the clause applies.

Hedging is a method of reducing portfolio risk or some business risks involving future transactions. Thus, the possible decline of a stock price can be hedged by buying a put for the stock. A business can hedge a foreign exchange transaction by purchasing a forward contract that guarantees the exchange rate for a future date.

Investors can reduce their liability risk in a business by forming a corporation, an corporation, or a limited liability company. This prevents the extension of the company's liabilities to its investors.

Methods of Risk Transfer

Apart from selling the asset there are three methods of transferring risks. These are also referred to as three dimensions of risk transfer. They are as follows,

(a) Hedging : Hedging is one of the method of transferring risk. When an individual's action reduces the exposure to a loss followed by giving up the possibility of gain of other party is known as hedging of risk. This could be understood with the help of following example,

Suppose a farmer agrees to sell a future harvest at a price fixed today. This eliminates the risk of low' price at the time of harvest and also the profit from high price at the time of harvest. Therefore, the price risk related to the crop is being hedged.

(b) Insuring : The payment of premium to avoid losses is known as insurance. Insurance substitutes a sure loss against the possibility of larger loss in the absence of insurance. Example: A car owner insures his car against the risk of damage or theft by paying a premium of ` 1000 today. By paying a premium and incurring a sure loss of ` 1000, he is substituting the possible losses that may cost hundred thousands of rupees.

Hedging eliminates the risk of loss by giving up the possibility of gain and insurance eliminates the risk of loss and retention of gain by payment of premium. This is one of the major difference between hedging and insuring.

Example: Suppose an British import/ export businessman is to receive \$100000 after a month. The pound price per \$ is £ (1). 80 at present. But, there is a possibility of change in exchange rate. The British businessman can manage the risk either through hedging, by entering into a contract to sell \$1,00,000 at the month end at a price £0.80 per dollar. This contract involves giving up of gain that may arise from increase in the price of pound over the dollar in the future.

On the other hand, he could insure the decline in the pound price against dollar by paying premium. In this case loss due to fall in price of pound can be avoided by exercising the option whereas increase, in the price of pound enables him to receive the benefit.

(c) Diversifying : Under this method similar amount of different risky assets are held, instead of holding an investment into a single risky asset. This is known as diversifying, as the risk is diversified among various risky assets. This would be explained with the help of following example: Suppose an individual plans to invest ` 1,00,000 in a technological business. Now he can either invest all ` 1,00,000 in one technological firm or invest in shares of technological firms, or several technological firms and so on. In this way the risk is diversified. Suppose he invested ` 20,000 in five different firms therefore the risk of winding up of any firm and loss is diversified.

5. **Insurance**

Insurance is another major method that most people, businesses, and other organizations can use to transfer pure risks, by paying a premium to an insurance company in exchange for a payment of a possible large loss. By using the law of large numbers, an insurance company can estimate fairly reliably the amount of loss for a given number of customers within a specific time. An insurance company can pay for losses because it pools and invests the premiums of many subscribers to pay the few who will have significant losses. Not every pure risk is insurable by private insurance companies.

Events which are unpredictable and that could cause extensive damage, such as earthquakes, are not insured by private insurers, although reinsurers may cover these types of risks by relying on statistical models to estimate the probabilities of disaster. Speculative risks are taken in the hope of making a profit are also not insurable, since these risks are taken voluntarily, and, hence, are not pure risks.

2.6 Risk Management and Steps Involved in it

Q25. Explain the concept of risk management.

Ans :

Risk management is the branch of the discipline '*management*' which is concerned with the overall management of risk and concerning aspects. More specifically, risk management is the study of identifying, analyzing, interpreting, and controlling of different economic risks which can endanger the individual or business organization.

''Define risk management as: The identification, analysis and economic control of those risks that can threaten the assets or earning capability of an enterprise.''

''Risk management is the systematic and efficient handling or pure risks.''

From the mentioned definitions above, it will be noted that these definitions emphasizes human effort and the organizational structure. Risk management similarly utilizes men, materials and machines in accomplishing its objectives, and furthermore, the application of risk management tools and the implementation of decisions in this area require highly trained personnel and proper equipment.

1. **Developing Specifications for the Coverage:** Risk management develop the specification for the coverage of loss or damages by a particular peril.
2. **Establishing Criteria for Handling Risk:** Risk management set the criterion on the basis of which it is possible to handle the arisen risk.
3. **Buying insurance at prices as low as possible, compatible with services desired:** Buying insurance is one of the major functions of a risk manager.
4. **Using insurers' and other agents' services effectively to deal with loss:** Efficient risk management always tries to utilize the insurer's services appropriately.
5. **Risk analysis:** Analyzing risk from a certain peril is the major work of risk management. After analyzing risk, it provides the possible directions on the basis of findings.
6. **Measurement of risk:** Every risk should be measured by its nature. Risk management functions to measure the probability of risk and give appropriate solution.
7. **Risk estimation:** Risk management estimates the possibility of risk by analyzing its criteria. Risk is obvious in every individual's life and in every business organization.
8. **Evaluating financial and business risk effectively:** Risk management evaluates risk both financial and business and tries to give the appropriate solution as possible.
9. **Risk handling:** To handling the risk of a certain peril the management of risk functions to get rid of the peril and tries to handle the risks in a proper manner.

10. **Risk controlling:** Risk management controls the risk and survives the individual or business entity by controlling the possible risk by precautionary measures.

11. **Achieving the risk management goal:** The risk management works to achieve the ultimate goal of the business entity as well.

12. **To decide the best and most economical method of handling the risk of loss:** Risk management decides the best and most economical method of handling the risk of different losses.

13. **To administer the programs of risk management:** Risk management administers and monitors the programs of risk management to perform smoothly.

14. **To estimate the frequency and size of loss:** To estimate the frequency and size of loss is another work of risk management.

These are the ultimate function which is being accomplished by risk management. The functions of risk management show the summary of risk management's function and its importance.

Q26. What are the steps involved in risk management process?

(OR)

Identify the steps in risk management process.

Ans : **(Imp.)**

The steps for achieving the risk management goal are :

1. To Identify or Discover the Risk Problems

The first step in risk management process is to identify or discover the risk problem or problems. In this stage

2. To Select Method/s Available to Solve the Problems

The second step in risk management process is to select the method or methods which match/s best with the handling of the certain risk arising from the peril or loss. This step includes four steps for selecting the method or methods, as,

(a) Risk avoidance

(b) Risk retention

(c) Loss control

(d) Risk transfer

3. To Choose which Method/s is/are the Most Efficient

The next step in the risk management process is to choose which method is the most appropriate for the specific type of risk.

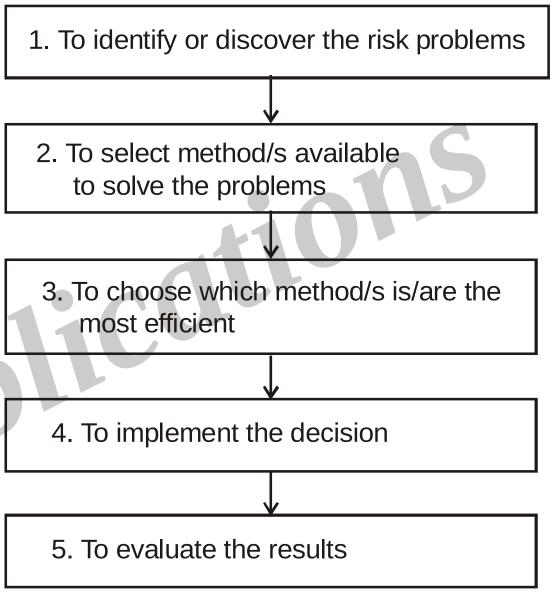


Fig. : The risk management process.

4. To Implement the Decision

The implementation of the decision of the risk must be done in this step. The proper implementation of the selected risk measurement tools should be reviewed and observed in this stage of risk management process.

5. To Evaluate the Results

The final step in the risk management procedure or process is to evaluate the result through observation, exit interview and supervision etc.

This is the risk management process through which one can get the possible result for the better handling of risk and other concerning materials.

Q27. What are the ways to determine the risk?

Ans :

As the premium of the insurance depends on the size and pattern of the insurance contract, the risk of the certain insurance policy is different from each other. So, on the basis of the acuteness of risk, we classify risk into four classes, as,

(a) Super standard risk

(b) Standard risk

(c) Sub-standard risk

(d) Un-insurable risk

(a) Super Standard Risk

In numerical ratting system of evaluating risk, some risks ranges 75 to less, is called super-standard risk. It is the expected risk in concern of insurer because the risk is minimum or nominal.

(b) Standard Risk

According to numerical ratting system of evaluating risk, rages 76 to 125, is called standard risk. That type of risk is natural or general.

(c) Sub-standard Risk

The risk which ranges from 126 to 500 is called sub-standard risk. The persons or business organizations who living with risky occupation, old building etc. are the sub-standard risk.

(d) Un-insurable Risk

When the policy amount is so high that is it exceeds the 500 and above is known as uninsurable risk for the business organisation or individual.

Super Standard Risk	Standard Risk	Sub-standard Risk	Un-insurable Risk
Below 75	From 76 to 125	From 126 to 500	From 501 to above

The risk should be taken considering some factors which actually affect or which should take care for the purpose of determining risk of a certain investment.

Q28. Describe the factors regarding which care should be taken in taking the risk for identification.

Ans :

Factors regarding which care should be taken in taking the risk for indemnification:

(a) Age: Age in life insurance is so important in consideration of the indemnification.

(b) Build/Body structure: Body structure of the insured person is important to consider the indemnification and the premium of the insurance.

(c) Physical condition: Physical condition is another way to consider the indemnification of the insured person.

(d) Personal history: History of personality is important for the determination of the indemnification of the certain type of insurance contract.

(e) **Family history:** History of family is another essential factor to get the indemnification of the insurance contract.

(f) **Occupation:** Occupation of the individual is deeply considered when the insurer consider the indemnity of the possible loss.

(g) **Residence:** Residence is also consider when there is taken step to make a insurance contract.

(h) **Present habits:** Habit of the individual should be taken into account because the individual may behave in a deviant way later.

(i) **Morale:** Morale of the individual portrays the shape of his or her attitude. So it will be effective to judge the appropriate manner of the concerned individual.

(j) **Race and nationality:** Race of the people and nationality of the persons help to determine the indemnification of the concerned insurance.

(k) **Sex:** Sex is another important factor which is considered to make an insurance.

(*l*) **Economic status:** Economic status is also helpful to consider about the indemnification of the insurance amount of premium.

(m) **Defence service:** If the insured has the defence services then it will be a positive for the indemnification.

(n) **Insurance plan:** Insurance plan also help to consider the risk thus, it help in considering the indemnification.

This is the brief discussion about the factors which care should be taken in taking the risk for indemnification.

Q29. Discuss the various methods of Evaluating risk.

Ans :

There are two methods of evaluating risk :

Man is social form the beginning of their life, but they always faces different difficult circumstance the situation generate different particular risk for the survival of man. Though the concept of risk is under the consideration of everyone but it is difficult to specify the consequence or acuteness of the risk. There are two general and all-recognized methods of evaluating risk, such as,

(a) Judgement Method of Evaluating Risk

In this process, the judgement from the health specialist, liability specialist and other insurance experts are considered as the means of judging the risk. Their judgement is so practical because the experts are very much conscious about the judgement and the judges are so experienced. In this way of judging risk, the insurer judges the age, sex, health, liability, property and the like.

(b) Numerical Ratting System of Evaluating Risk

In number ratting system, the risk is evaluated in the form of a range table. If any risk level comprises into a specific range then the risk would be of that standard risk. For example,

As the premium of the insurance depends on the size and pattern of the insurance contract, the risk of a certain insurance policy is different from each other. So, on the basis of the acuteness of risk, we classify risk into four classes, as,

(i) Super standard risk

(ii) Standard risk

(iii) Sub-standard risk

(iv) Un-insurable risk

(i) Super standard risk: In numerical ratting system of evaluating risk, some risks ranges 75 to less, is called super-standard risk. It is the expected risk in concern of insurer because the risk is minimum or nominal.

(ii) Standard risk: According to numerical ratting system of evaluating risk, rages 76 to 125, is called standard risk. That type of risk is natural or general.

(iii) Sub-standard risk: The risk which ranges from 126 to 500 is called sub-standard risk. The persons or business organizations who living with risky occupation, old building etc. are the sub-standard risk.

(iv) Un-insurable risk: When the policy amount is so high that is it exceeds the 500 and above is known as uninsurable risk for the business organisation or individual.

Super Standard Risk	Standard Risk	Sub-standard Risk	Un-insurable Risk
Below 75	From 76 to 125	From 126 to 500	From 501 to above

This is the way to evaluate risk of a certain type.

Q30. Discuss the methods/ways/techniques of handling risk.

Ans :

Risk

Methods of dealing with economic risks faced by different business organizations may be classified under six categories :

1. **Risk may be avoided:** Risk, if it is possible, should be avoided. This is the most suggested methods of handling risk.
2. **Risk may be retained:** Risk retention or retaining from risk is another way of handling risk.
3. **Hazard may be reduced:** Reduction of situation which is hazardous and simply put the function of an individual or business organisation as a whole.
4. **Loss may be reduced:** Losses from different sources should be reduced if possible.
5. **Risk may be shifted:** By shifting the risk to another insurer, it is possible to shift the risk of the firm or individual.
6. **Risk may be reduced:** The risk may be reduced by the elimination of the risk.

2.7 Concept of Claim

Q31. Define claim. What are the features of claims?

Ans :

Meaning

As insurance claim is a formal request to an insurance company for coverage or compensation for a covered loss or policy event. The insurance company validates the claim and, once approved, issue payment to the insured or an approved interested party on behalf of the insured.

Insurance claims cover everything from death benefits on life insurance policies to routine and comprehensive medical exams. In many cases, third-parties file claims on behalf of the insured person, but usually only the person(s) listed on the policy is entitled to claim payments.

A paid insurance claim serves to indemnify a policysholder against financial loss. An individual or group pays previous as consideration for completion of an insurance contract between the insured party and an insurance carrier. The most common insurance claims involve costs for medical goods and services, physical damage and liability resulting from the operation of automobiles, property damage and liability for dwellings (homeowners, landlords, and renters), and the loss of life.

Features

1. It covers everything i.e., from doctors consultation fees to the death expenses of a person.
2. It serves to indemnify the policy holder against financial loss.
3. It is a formal request of policy holder to insurance company for compensating the losses suffered.
4. It vary depending upon the nature of insurance policy. For example, life insurance claim, property insurance claim etc.
5. It is compulsory while claiming for any loss, insurer need to provide enough evidences for the financial loss occurred. For example, ownership of claimed items, medical reports etc.

Q32. What are the different types of life insurance claims ?

Ans :

The life insurance claims are divided into three types,

The basic necessity for settlement of claim arises on death of the policy holder or maturity of policy.

1. Death Claim

The death claim arises on the death of the policy holder. Death can be natural, accidental or a suicide. Death claim is further classified as,

(i) Premature Claim : In case of premature claim, insured person dies within three (3) years from the date on which insurance policy is taken.

(ii) Other Claim : In case of other claim, insured person dies after three (3) years from the date on which insurance policy is taken.

2. Maturity Claim

The essential features of maturity claims are listed below,

(a) A maturity claim is payable according to the conditions of the contract the completion of the policy term period, if the insured person is alive till the maturity date.

(b) This claim includes the assured sum, vested bonuses and other specified money. Any debt or charge under the policy such as outstanding premia and loans will be deducted from the assured sum.

(c) When it comes to proof of title, settlement of maturity claims is quite easy as the policy money is paid directly to the insured person itself.

(d) The insurance company makes payment to the absolute assignee in case of an absolute assigned policy.

(e) Policy holders are informed in advance about the maturity date by the insurers. The insurers also send the discharge form to the policy holders and request them to return the discharge form signed, duly stamped and enclosed with the documents such as,

(i) The policy document

(ii) Age proof (if age is not admitted yet)

(iii) In case if an assignment is made the stamped document of assignment should also be submitted.

3. Survival Benefit Payment

Some policies such as money back policies allow the insured person for the survival benefit before the full term policy expires. Settlement of the survival benefit is less complicated when compared to settlement of maturity claim.

The procedure for settlement of survival benefit is as follows,

(i) Insurer intimates the policy holder in advance about the money back policies and sends a discharge voucher.

(ii) The policy holder returns the documents duly stamped and signed and witnessed with the original policy document for necessary approval.

(iii) The gross amount is nothing but the installments of the sum of money assured payable.

(iv) After subtracting the outstanding premium, outstanding loan interest etc., from the gross amount, the net amount is arrived.

Q33. What are the different types of Non-life insurance claim.

Ans :

There are two types of General Insurance or Non-life Insurance claims. They are,

1. Motor Insurance Claim, and
2. Property Insurance Claim.

1. Motor Insurance Claim

Motor insurance policy claim occurs when any damage caused to the policyholder vehicle either by fire, accident or theft.

2. Property Insurance Claim

Property insurance claim occurs when there is any loss or damage caused to the property due to fire, lightning, windstorm, hurricane, earthquake or tornado.

2.7.1 Understanding the Process of Claim Management

Q34. What are the various steps involved in Claim Management?

Ans : **(Imp.)**

Notice of fire: As soon as the fire occurs, the insured must send a notice of loss in writing to the insurance company. If possible, he must submit the evidences of loss and the evidence he did everything to mitigate the loss. If deliberate arson is suspected, an FIR must be lodged with the police and a copy of FIR must be submitted along with the notice.

1. Submission of Claim

After receiving the notice of fire, the insurance company sends a claim form to the insured. The insured should carefully fill the form as the details given in the form can affect the amount of the claim. Any wrong information can result in the refusal of the claim.

2. Inspection of the Property

The insurance company may send an examiner or an inspector to examine the loss. The inspector makes an inspection and submits it to the company.

3. Assessment of the Loss

After getting the report, the insurance company appoints an agent or an assessor to determine the value of the loss that has to be compensated.

4. Payment of the Claim

The insurance company makes payment to the insured on the basis of the report of the assessor.

It may also reject the claim on the following grounds:

(a) The claim is fraudulent.

(b) The loss was not covered by the fire.

(c) The loss occurred due to defect in the insured property not disclosed at the time of taking up the policy.

(d) The loss was not intentional.

(e) The insured has no insurable interest at the time of the loss.

2.7.2 Claims Fraud and Fraud Prevention

Q35. Explain briefly about Claims Fraud and Fraud Prevention.

Ans :

Insurance fraud affects not only the financial health of the insurers, but also of innocent people seeking effective insurance coverage. Fraudulent claims are a serious financial burden on insurers and result in higher overall insurance costs. Insurance fraud costs companies billions of dollars per year across the globe, making it imperative that insurers take a proactive stance against fraud. Insurance companies should establish a technology framework, tap into advanced automation and analytics, and take steps to prevent it.

Here are a few examples of the way data analysis can be applied to fight fraud in the insurance industry:

1. Medical Billing Fraud

Identify excessive billing - same diagnosis, same procedure Identify excessive number of procedures, per day or place of service/day Identify multiple billing of same procedure, same date of service Locate age inappropriate treatments - too young/old for treatment Identify duplicate charges on patient bills Find doctor and patient with same address

2. Claims Fraud

- Identify duplicate claims
- Review submission of multiple/inflated claims
- Find fraudulent family members: i.e., five dependent children born within a two year period.
- Highlight incorrect gender specific treatments
- Flag mutually exclusive procedures: e.g. if appendix removed on 01/10/14, then it would be impossible to have appendicitis on 01/02/15.
- Highlight failure to disclose pre-existing condition (where applicable)

3. Life Insurance Fraud

- Determine patterns of overpayment of premiums.
- Review transaction payments comprising more than one type of payment instrument.
- Report multiple accounts to collect funds or payment to beneficiaries.
- Report purchase of multiple products in a short period of time.
- Review beneficiaries with multiple policies.
- Isolate transactions for follow-up where employees are beneficiaries.
- Determine agents/brokers with statistically high numbers of claim payouts.
- Calculate benefit payments paid for lapsed policies.
- Find policy loans that are greater than face value.
- Report unauthorized policy changes.
- Identify missing, duplicate, void or out-of-sequence check numbers.

Steps for Preventing Insurance Fraud

To avoid expensive litigation and other costly measures, it is essential that insurance companies move forcefully against fraud. This begins by adopting a proactive stance toward fraud detection. Companies should not wait for fraud to occur and deal with it after the fact; instead, they should take actions and implement processes that identify potential fraud early and provide the ability to move quickly when fraud is detected.

Moving from reactive to proactive fraud detection takes six steps:

1. Implement a Foundational Framework

A foundational framework should reflect a fraud-detection strategy that addresses such questions as: How can we check all claims for fraud but ensure fast claim processing? How can we identify fraud before a claim is paid? How can we improve fraud investigation efficiency? How can we keep track of changing fraud behaviors? How can we reduce false positive signals? And finally: What is the best approach to automate the fraud-detection process and predict the likelihood of fraud? Implementing a foundational framework enables management to make better decisions about priorities, resource deployment and investments.

A foundational framework can range from an “out-of-the-box” solution that automates the institutional knowledge of your claims professionals and enables workflow management to full social networking analysis of the parties involved in a claim. From there, insurers can add a multitude of scoring engines, third-party data captures, criminal history lookups and many other tools. An important aspect of fraud detection is having a culture in your claims staff that emphasizes the importance of recognizing, identifying and investigating suspicious claims. Empower your staff to be involved and then the tools you deploy will function much more effectively.

2. Know the Relative Level of Fraud Potential

Knowing the relative level of fraud potential for every type of claim allows the best, and quickest, action to be taken to maximize special investigative unit (SIU) efficiency and savings. With limited resources to devote to fraud, it is important to make sure your investigations can be focused on the items that have the greatest potential for cost avoidance and successful identifications.

For example, a theft claim involving the suspicious disappearance of expensive jewelry has a higher potential for being fraudulent than a stolen smart phone or laptop. Examples of common false claim schemes include deliberately destroying property and mis reporting the cost of auto repairs.

3. Use Data Analytics to Detect Fraud

Fraud comes in all shapes and sizes. In general, insurance fraud can be divided into two categories: criminal fraud, which is perpetrated by professionals habitually trying to milk the system and cultural fraud, which is a genuine claimant being opportunistic or exaggerating a claim.

Data analytics can be applied to detect fraud. By analyzing past fraud, insurers can use predictive modeling to produce what is called a "Suspicion Score," a value for the propensity of fraud. The process works like this: Adjusters simply enter data, and claims are automatically given a Suspicion Score to indicate the likelihood that fraud has occurred. The technology behind this involves utilizing data-mining tools and applying quantitative analysis.

Even with automation and data analytics, the weakest link in fighting fraud can be your own employees. The importance of checks and balances cannot be stressed enough.

4. Continually Review and Rescore Claims

Success in combating insurance fraud comes from persistence and good timing. Above all, apply your arsenal of tools including data analytics and predictive modeling early and often. Claims should be continuously monitored for fraud potential. As an insurance company, it is imperative that you target the right claims, at the right time, with the right tools. Luckily, predictive modeling and advanced analytics are coming into play as essential tools for fighting insurance fraud. These tools can be automated, preventing the need for hands-on manual analysis.

By continuously reviewing and rescoring claims using Suspicion Scores, insurers can detect patterns that reveal fraud. Some claims score high immediately at first notice of loss, prompting your SIU to get involved immediately. For others, high scores do not show up until after the claim has been collected.

Monitoring Suspicion Scores has been shown to be more accurate and more effective than traditional fraud-detection methods. But again, the key is to not rely solely on technology to do all of the heavy lifting - human analysts are required to initiate action after the suspected fraud has been flagged, and your people must follow through with appropriate measures. This is where training employees to identify fraud becomes an important piece of the overall fraud-detection puzzle.

5. Adopt a Layered Approach

In the world of IT, a "layered approach" refers to using a variety of tools and technologies to tackle a challenge. In detecting insurance fraud, this means throwing the kitchen sink at the criminals, but doing it in an organized, well-considered fashion. Fraud is a complex, multifaceted problem, and no single method can detect all fraud. Each fraud-detection method needs to be crafted to address a specific area. Different rules and indicators are needed for different types of policies and claims. Plus, fraudsters hide in multiple databases, so fraud-detection methods must search them all. Because of the complexity of fighting fraud, it is advisable to bring in outside expertise to help formulate a framework and implement the technology, tools and methods needed to deal effectively with fraud.

The modern insurance organization has a number of technology tools at its disposal to detect fraud. For example, videos, photos and even livestreaming can be used to document evidence at a car crash or crime scene. It's difficult for the average person to fake a video, especially when the device's location access is turned on. A virtual gold mine lies within unstructured data, and it is imperative to collect, organize, index and mine the data to detect fraud. Always remember: You can't claim what you can't prove.

6. Revise Based on Market Conditions

Criminals are ever resourceful, so always be ready to quickly adapt to changes in the ways fraud is undertaken, as well as changes in your industry. For example, professional criminals are sophisticated enough to become familiar with the analytical approaches that insurance companies use to detect fraud, and to change their tactics when committing fraud. As fighting fraud becomes more proactive, insurers must spot new fraud trends early and take steps to stay ahead of the bad guys.

2.8 Insurance Reserves

Q36. Define the following terms :

(i) Reserves

(ii) Insurance Reserves

Ans : **(Imp.)**

(i) Reserves: According to the American Institute of Accounting, "the use of the term reserve by limited to indicate, that an undivided part of the asset is being held or retained for general or specific reserve". This in simple terms, reserve can be defined as "A part of the profit which is kept aside by the firm to meet up any future contingency, liability or make adjustment for the decrease in the value of an asset".

(ii) Insurance Reserves: Insurance reserve refers to the monetary reserve which is set aside by insurance companies to pay for claims by their customers. This, is known as insurance reserve. Thus, in simple words, it refers to the financial reserves which are maintained by every type of insurance organization.

2.8.1 Different Types of Reserves of Insurance Companies

Q37. State the purpose and types of insurance reserves.

Ans :

Purpose of Insurance Reserve

Insurance reserves are generally used for the following purpose,

(a) To be used for claims made by their customers.

(b) To be used for sudden financial contingencies.

(c) To improve the firms overall liquidity and financial status.

(d) To help towards expansion of the business.

(e) To adhere to the legal provisions of maintaining reserves.

Types of Insurance Reserves

Insurance companies generally maintain the following types of insurance reserves,

1. Claims Reserve

This is the most common type of reserve which is maintained by all kinds of insurance companies. It is the reserve from which the insurance company pay for the claims made by its customers. Whenever any customer makes a claim to the insurance company, the claim adjuster opens a claim file and initiates documentation for the claim. Finally the amount to be paid towards the claim and all related expenses are deducted from the claims reserve.

This is the most common and important type of insurance reserve and it is used to measure the year end profitability of the insurance company.

2. IBNR Reserve

IBNR stands for Incurred But Not Reported. It refers to those insurance claims which are incurred and need to be paid by the insurance company, however the insured customer or their nominee had not yet initiated the claim. For example, Mr A took an accidental insurance for ? 50 lakhs. After some time, Mr A dies in a road accident. The family of Mr. A did not claim the insurance money for 2 years. In this case, ones Mr. A had expired in the road accident, it becomes IBNR.

Insurance firms set aside IBNR reserves to provide for old big claims.

3. Statutory Insurance Reserve

It refers to the statutory/mandatory reserves which an insurance company needs to maintain as per legal guidelines prescribed by the government. Maintaining of such reserve ensures that the insurance company remains solvent even when huge financial claims are made by customers.

4. Fluctuation Reserve

It is common for an insurance firm to experience fluctuation towards claims made. Thus a separate fluctuation reserve is maintained which can be used in case there are unexpectedly high number of insurance claims made to the insurance company.

5. Disaster Reserve

Many insurance companies maintain a substantial amount of reserve in the name of disaster reserve. Generally if there occurs any natural disaster such as earthquake, floods etc, there would be a very large number of claims, to be settled. This reserve protect the insurance firm against sudden large number of claims in case of any natural disaster.

6. Unexpired Risk Reserve

This reserve is maintained on the assumption that insurance premium may not be alone sufficient to cover the cost of risk and expenses. Therefore, insurance firms maintain this reserve.

2.9 Insurance Accounting

Q38. Define Insurance Accounting. State the recent developments of insurance accounting.

Ans :

Meaning

The accounting process followed by insurance companies for maintaining their accounts of clients and claims is referred as insurance accounting. General insurance companies maintains accounting books as per the guidelines given by Insurance Regulatory and Development Authority (IRDA).

Recent Developments

Recent Developments of Insurance Accounting are :

1. Insurance Contracts

It appears unlikely that the U.S. Financial Accounting Standards Board (FASB) and the International Accounting Standard Board (IASB) will be able to achieve a convergence of the two systems with regard to property/casualty insurance. In February 2014 Accounting Today reported that FASB decided to focus on improving U.S. GAAP instead of continuing with the convergence project. For short-duration contracts - which includes most property/casualty insurance - FASB will target changes that enhance disclosures. For long-duration contracts like life insurance, the board concluded it should consider IASB's approach, though the auditing and consulting firm of Deloitte notes that even in this regard convergence is not the primary objective of the changes.

2. Financial Reporting

An SEC report published in July 2012 made no recommendations about whether the IFRS should be incorporated into the U.S. financial reporting system although it did say that there was little support among major U.S. corporations for adopting the IFRS as authoritative guidance.

3. Insurance Basics

Insurers assume and manage risk in return for a premium. The premium for each policy or contract, is calculated based in part on historical data aggregated from many similar policies and is paid in advance of the delivery of the service. The actual cost of each policy to the insurer is not known until the end of the policy period (or for some insurance products long after the end of the policy period), when the cost of claims can be calculated with finality.

4. The Insurance Industry is divided into two major Segments

Property/casualty also known as general insurance or nonlife, particularly outside the United States and life/health. Broadly speaking, property/casualty policies cover homes, autos and businesses; life/health insurers sell life, long-term care and disability insurance, annuities and health insurance. U.S. insurers submit financial statements to state regulators using statutory accounting principles, but there are significant differences between the accounting practices of property/casualty and life insurers due to the nature of their products. These include:

5. Contract Duration

Property/casualty insurance policies are usually short-term contracts, six-months to a year. Their final cost will usually be known within a year or so after the policy term begins, except for some types of liability contracts. They are known as short- duration contracts. By contrast, life, disability and long-term care insurance and annuity contracts are typically long-duration contracts - in force for decades.

6. Variability of Claims Outcomes Per Year

The range of potential outcomes with property/casualty insurance contracts can vary widely, depending on whether claims are made under the policy, and if so, how much each claim ultimately settles for. The cost of investigating a claim can also vary. In some years, natural disasters such as hurricanes and man-made disasters such as terrorist attacks can produce huge numbers of claims. By contrast, claims against life insurance and annuity contracts are typically amounts stated in the contracts and are therefore more predictable. There are few instances of catastrophic losses in the life insurance industry comparable to those in the property/ casualty insurance industry.

7. Financial Statements

An insurance company's annual financial statement is a lengthy and detailed document that shows all aspects of its business. In statutory accounting, the initial section includes a balance sheet, an income statement and a section known as the Capital and Surplus Account, which sets out the major components of policyholders' surplus and changes in the account during the year.

As with GAAP accounting, the balance sheet presents a picture of a company's financial position at one moment in time its assets and its liabilities and the income statement provides a record of the company's operating results from the previous period. An insurance company's policyholders' surplus its assets minus its liabilities serves as the company's financial cushion against catastrophic losses and as a way to fund expansion. Regulators require insurers to have sufficient surplus to support the policies they issue. The greater the risks assumed, and hence the greater the potential for claims against the policy, the higher the amount of policyholders' surplus required.

8. Asset Valuation

Property/casualty companies need to be able to pay predictable claims promptly and also to raise cash quickly to pay for a large number of claims in case of a hurricane or other disaster. Therefore, most of their assets are high quality, income- paying government and corporate bonds that are generally held to maturity. Under SAP, they are valued at amortized cost rather than their current market cost. This produces a relatively stable bond asset value from year to year (and reflects the expected use of the asset.

9. Liabilities and reserves

Liabilities or claims against assets, are divided into two components: reserves for obligations to policyholders and claims by other creditors. Reserves for an insurer's obligations to its policyholders are by far the largest liability. Property/casualty insurers have three types of reserve funds: unearned premium reserves, or pre-claims liability; loss and loss adjustment reserves, or post claims liability; and other.

Q39. Explain the preparation of various accounts of General insurance.

(OR)

How is the revenue account of General insurance companies prepared?

(OR)

How is the profit and loss account of General insurance companies prepared?

(OR)

How is the balance sheet of General insurance companies prepared?

Ans : **(Imp.)**

1. Revenue Account

Revenue Account for the Year Ended 31st March, 20...

Policyholders' Account (Technical Account)

S.No.	Particulars	Schedule No.	Current Year (` '000)	Previous Year (` '000)
A. 1.	Premiums Earned (Net)	1		
2.	Profit/Loss on Sale /Redemption of Investments			
3.	Others (to be specified)			
4.	Interest, Dividend & Rent—Gross			
	Total (A)			
B. 1.	Claims Incurred (Net)	2		
2.	Commission	3		
3.	Operating Expenses related to Insurance Business	4		
	Total (B)			
C.	Operating Profit/(Loss) from Fire/ Marine / Miscellaneous Business = (A-B)			
D.	**Appropriations**			
	Transfer to Shareholders' Account			
	Transfer to Catastrophe Reserve			
	Transfer to Other Reserves (to be specified)			
	Total of (C)			

2. Profit and Loss Account

Profit and Loss Account for the Year Ended 31st March, 20...

Shareholders' Account (Non-technical Account)

S.No.	Particulars	Schedule No.	Current Year ` ('000)	Previous Year ` ('000)
1.	**Operating Profit / (Loss)**			
	(a) Fire Insurance			
	(b) Marine Insurance			
	(c) Miscellaneous Insurance			
2.	Income from investments			
	(a) Interest, Dividend & Rent - Gross			
	(b) Profit on Sale of Investments			
	Less : Less on sale of Investments			
3.	**Other Income** (To be specified)			
	TOTAL (A)			
4.	**Provisions (Other than taxation)**			
	(a) For Diminution in the Value of Investments			
	(b) For Doubtful Debts			
	(c) Others (to be specified)			
5.	Other Expenses			
	(a) Expenses other than those related to Insurance Business			
	(b) Bad Debts written off			
	(c) Others (to be specified)			
	Total (B)			
	Profit before Tax			
	Provision for Taxation			
	Profit after Tax			
	Appropriations			
	(a) Interim Dividends paid during the year			
	(b) Proposed Final Dividend			
	(c) Dividend distribution tax			
	(d) Transfer to Reserves or other Accounts (to be specified)			
	Balance of Profit/Loss brought forward from last year			
	Balance carried forward to Balance Sheet			

Notes : To Form B-RA and B PL

(a) Premium income received from business concluded in and outside India shall be separately disclosed.

(b) Reinsurance premiums whether on business ceded or accepted are to be brought into account gross (i.e., before deducting commissions) under the head reinsurance premiums.

(c) Claims incurred shall comprise claims paid, specific claims settlement costs wherever applicable and change in the outstanding provisions for claims at the year-end.

(d) Items of expenses and income in excess of one per cent of the total premiums (less reinsurance) or ` 5,00,000 whichever is higher, shall be shown as a separate line item.

(e) Fees and expenses connected with claims shall be included in claims.

(f) Under the sub-head "Others" shall be included items like foreign exchange gains or losses and other items.

(g) Interest, dividends and rentals receivable in connection with an investment should be stated at gross amount, the amount of income tax deducted at source being included under 'advance taxes paid and taxes deducted at source".

(h) Income from rent shall include only the realized rent. It shall not include any notional rent.

3. Balance Sheet

Balance Sheet as at 31st March 20....

S.No.	Particulars	Schedule No.	Current Year ` ('000)	Previous Year ` ('000)
I.	**Sources of Funds**			
	Share Capital	5		
	Reserves and Surplus	6		
	Fair Value Change Account			
	Borrowings	7		
	Total			
II.	**Application of Funds**			
	Investments	8		
	Loans	9		
	Fixed Assets	10		
	Current Assets – A			
	Cash and Bank Balances	11		
	Advances and Other Assets	12		
	Sub-total (A)			
	Current Liabilities – B	13		
	Provisions	14		
	Sub-Total (B)			
	Net Current Assets (C) = (A - B)			
	Miscellaneous Expenditure (to the extent not written off or adjusted)	15		
	Debit Balance in Profit & Loss Account			
	Total			

Contingent Liabilities

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Partly paid-up investments		
2.	Claims, other than against policies, not acknowledged as debts by the company		
3.	Underwriting commitments outstanding (in respect of shares and securities)		
4.	Guarantees given by or on behalf of the Company		
5.	Statutory demands/ liabilities in dispute, not provided for		
6.	Reinsurance obligations to the extent not provided for in accounts		
7.	Others (to be specified)		
	Total		

Q40. Explain the various schedules which are to be prepared as a part of final account of General Insurance companies

Ans :

SCHEDULE 1 – Premium Earned [Net]

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
	Premium from direct business written		
	Add: Premium on reinsurance accepted		
	Less : Premium on reinsurance ceded		
	Net Premium		
	Adjustment for change in reserve for unexpired risks		
	Total Premium Earned (Net)		

Note : Reinsurance premiums whether on business ceded or accepted are to be brought into account, before deducting commission under the head of reinsurance premiums.

SCHEDULE 2 – Claims Incurred [Net]

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
	Claims paid		
	Direct		
	Add: Re-insurance accepted		
	Less : Re insurance ceded		
	Net Claims paid		
	Add : Claims outstanding at the end of the year		
	Less : Claims outstanding at the beginning		
	Total Claims incurred		

Notes :

(a) Incurred But Not Reported (IBNR). Incurred but not enough reported (IBNER) claims should be included in the amount for outstanding claims.

(b) Claims include specific claims settlement cost but not expenses of management.

(c) The surveyor fees, legal and other expenses shall also form part of claims cost.

(d) Claims cost should be adjusted for estimated salvage value if there is a sufficient certainty of its realization.

SCHEDULE 3 – Commission

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
	Commission paid Direct		
	Add: Re-insurance Accepted		
	Less : Commission on Re-insurance Ceded		
	Net Commission		

Note : The profit / commission, if any, are to be combined with the Re-insurance accepted or Re-insurance ceded figures

Schedule 4 – Operating Expenses Related to Insurance Business

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Employees' remuneration & welfare benefits		
2.	Travel, conveyance and vehicle running expenses		
3.	Training expenses		
4.	Rents, rates & taxes		
5.	Repairs		

6.	Printing & stationery		
7.	Communication		
8.	Legal & professional charges		
9.	Auditors' fees, expenses etc.		
	(a) as auditor		
	(b) as adviser or in any other capacity, in respect of:		
	(i) Taxation matters		
	(ii) Insurance matters		
	(iii) Management services; and		
	(c) in any other capacity		
10.	Advertisement and publicity		
11.	Interest & Bank Charges		
12.	Others (to be specified)		
13.	Depreciation		
	Total		

Note : Items of expenses and income in excess of one per cent of the total premiums (less reinsurance) or ` 5,00,000 whichever is higher, shall be shown as a separate line item.

SCHEDULE 5 – Share Capital

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Authorized Capital		
	Equity Shares of ` .... each		
2.	Issued Capital		
	Equity Shares of ` .... each		
3.	Subscribed Capital		
	Equity Shares ` .... each		
4.	Called-up Capital		
	Equity Shares of ` .... each		
	Less: Calls unpaid		
	Add: Equity Shares forfeited (Amount originally paid up)		
	Less : Par Value of Equity Shares bought back		
	Less : Preliminary Expenses		
	Expenses including commission or brokerage on underwriting or subscription of shares		
	Total		

Notes :

(a) Particulars of the different classes of capital should be separately stated.

(b) The amount capitalised on account of issue of bonus shares should be disclosed.

(c) In case any part of the capital is held by a holding company, the same should be separately disclosed.

SCHEDULE 5A – Share Capital Pattern Of Shareholding

[As certified by the Management]

Shareholder	Current Year		Previous Year	
	Number of Shares	% of Holding	Number of Shares	% of Holding
Promoters				
(i) Indian				
(ii) Foreign				
Others				
Total				

SCHEDULE 6 – Reserves And Surplus

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Capital Reserve		
2.	Capital Redemption Reserve		
3.	Securities Premium		
4.	General Reserves		
	Less : Debit balance in Profit and Loss Account		
	Less : Amount utilized for Buy-back		
5.	Catastrophe Reserve		
6.	Other Reserves (to be specified)		
7.	Balance of Profit in Profit and Loss Account		–
	Total		

Note : Additions to and deductions from the reserves should be disclosed under each of the specified heads.

SCHEDULE 7 – Borrowings

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Debentures/Bonds		
2.	Banks		
3.	Financial Institutions		
4.	Others (to be specified)		
	Total		

Note :

(a) The extent to which the borrowings are secured shall be separately disclosed stating the nature of the security under each sub-head.

(b) Amounts due within 12 months from the date of Balance Sheet be shown separately.

SCHEDULE 8 – Investments

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
	LONG TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		
3.	Other Investments		
	(a) Shares		
	(aa) Equity		
	(bb) Preference		
	(b) Mutual Funds		
	(c) Derivative Instruments		
	(d) Debentures/ Bonds		
	(e) Other Securities (to be specified)		
	(f) Subsidiaries		
	(g) Investment Properties-Real Estate		
4.	Investments in Infrastructure and Social Sector		
5.	Other than Approved Investments		

	SHORT TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		
3.	Other Investments		
	(a) Shares		
	(aa) Equity		
	(bb) Preference		
	(b) Mutual Funds		
	(c) Derivative Instruments		
	(d) Debentures/ Bonds		
	(e) Other Securities (to be specified)		
	(f) Subsidiaries		
	(g) Investment Properties-Real Estate		
4.	Investments in Infrastructure and Social Sector		
5.	Other than Approved Investments		
	Total		

Notes :

(a) Investments in subsidiary/holding companies, joint ventures and associates shall be separately disclosed, at cost.

(i) Holding company and subsidiary shall be construed as defined in the Companies Act. 1956.

(ii) Joint Venture is a contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control.

(iii) Joint control – is the contractually agreed sharing of power to govern the financial and operating policies of an economic activity to obtain benefits from it.

(iv) Associate – is an enterprise in which the company has significant influence and which is neither a subsidiary nor a joint venture of the company.

(v) Significant influence (for the purpose of this schedule)—means participation in the financial and operating policy decisions of a company, but not control of those policies. Significant influence may be exercised in several ways.

(b) Aggregate amount of company’s investments other than listed equity securities and derivative instruments and also the market value thereof shall be disclosed.

(c) Investment made out of Catastrophe reserve should be shown separately.

(d) Debt securities will be considered as “held to maturity” securities and will be measured at historical costs subject to amortisation.

(e) Investment property means a property [land or building or part of a building or both] held to earn rental income or for capital appreciation or for both, rather than for use in services or for administrative purposes.

(f) Investments maturing within twelve months from balance sheet date and investments made with the specific intention to dispose of within twelve months from balance sheet date shall be classified as short-term investments.

SCHEDULE 9 – LOANS

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	**Security-wise Classification**		
	Secured		
	(a) On Mortgage of Property		
	(i) In India		
	(ii) Outside India		
	(b) On Shares, Bonds, Govt. Securities, etc.		
	(c) Others (to be specified)		
	Unsecured		
	Total		
2.	**Borrower-wise Classification**		
	(a) Central and State Governments		
	(b) Banks and Financial Institutions		
	(c) Subsidiaries		
	(d) Industrial Undertakings		
	(e) Others (to be specified)		
	Total		
3.	**Performance-wise Classification**		
	(a) Loans Classified as Standard		
	(i) In India		
	(ii) Outside India		
	(b) Non-performing Loans less Provisions		
	(i) In India		
	(ii) Outside India Total		
4.	**Maturity-wise Classification**		
	(a) Short Term		
	(b) Long Term		
	Total		

Notes :

(a) Short-term loans shall include those, which are repayable within 12 months from the date of balance short. Long term loans shall be the loans other than short-term loans.

(b) Provisions against non-performing loans shall be shown separately.

(c) The nature of the security in case of all long term secured loans shall be specified in each case. Secured loans for the purposes of this schedule, means loans secured wholly or partly against an asset of the company.

(d) Loans considered doubtful and the amount of provision created against such loans shall be disclosed.

SCHEDULE 10 – Fixed Assets

Particulars		Cost/Gross Block			Depreciation				Net Block	
	Open -ing	Addit- ions	Deduct- ions	Closing	Upto Last Year	For the Year	On Sales/ Adjust- ments	To Date	As at year end	Previous Year
	Rs.('000)	Rs.('000)	Rs.('000)	Rs.('000)	Rs.('000)	Rs.('000)	Rs.('000)	Rs.('000)	Rs.('000)	Rs.('000)
Goodwill										
Intangibles (specify)										
Land-Freehold										
Leasehold Property										
Buildings										
Furniture & Fittings										
Information Technology Equipment										
Vehicles										
Office Equipment										
Others (Specify nature)										
Total										
Work-in-progress										
Grand Total										
Previous Year										

Note : Assets included in land, building and property above exclude Investment Properties as defined in note (e) to Schedule 8.

SCHEDULE 11 – Cash And Bank Balances

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Cash (including cheques, drafts and stamps)		
2.	Bank Balances		
	(a) Deposit Accounts		
	(i) Short-term (due within 12 months)		
	(ii) Others		
	(b) Current Accounts		
	(c) Others (to be specified)		
3.	Money at Call and Short Notice		
	(a) With Banks		
	(b) With Other Institutions		
4.	Others (to be specified)		
	Total		
	Balances with non-scheduled banks in 2 and 3 above		

Note : Bank balance may include remittances in transit. If so, the nature and amount shall be separately stated.

SCHEDULE – 12 Advances And Other Assets

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
A.	**Advances**		
1.	Reserve deposits with ceding companies		
2.	Application money for investments		
3.	Prepayments		
4.	Advances to Directors/Officers		
5.	Advance tax paid and taxes deducted at source (Net of provision for taxation)		
6.	Others (to be specified)		
	Total (A)		

B.	**Others Assets**		
1.	Income accrued on Investments		
2.	Outstanding Premiums		
3.	Agents' Balances		
4.	Foreign Agencies Balances		
5.	Due from other entities carrying on insurance business (including reinsurers).		
6.	Due from subsidiaries/holding		
7.	Deposit with Reserve Bank of India		
8.	Others (to be specified)		
	Total (B)		
	Total (A + B)		

Notes :

(a) The items under the above heads shall not be shown net of provisions for doubtful amounts. The amount of provision against each head should be shown separately.

(b) The term 'officer' should conform to the definition of that term as given under the Companies Act. 1956.

(c) Sundry debtors will be shown under item 8 (Others).

SCHEDULE – 13 Current Liabilities

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Agents' Balances		
2.	Balances due to other insurance companies		
3.	Deposits held on re-insurance ceded		
4.	Premiums received in advance		
5.	Unallocated premium		
6.	Sundry creditors		
7.	Due to subsidiaries/holding company		
8.	Claims outstanding		
9.	Due to officers/directors		
10.	Others (to be specified)		
	Total		

SCHEDULE–14 Provisions

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Reserve for Unexpired Risk		
2.	For taxation (less advance tax paid and taxes deducted at source)		
3.	For proposed dividends		
4.	For dividend distribution tax		
5.	Others (to be specified)		
	Total		

SCHEDULE–15

Miscellaneous Expenditure

(To the extent not written off or adjusted)

S.No.	Particulars	Current Year ` ('000)	Previous Year ` ('000)
1.	Discount Allowed on issue of shares/debentures		
2.	Others (to be specified)		
	Total		

Notes :

(a) No item shall be Included under the head "Miscellaneous Expenditure" and carried forward unless:

1. Some benefit from the expenditure can reasonably be expected to be received in future, and
2. The amount of such benefit is reasonably determinable.

(b) The amount to be carried forward in respect of any item included under the head "Miscellaneous Expenditure" shall not exceed the expected future revenue/other benefits related to the expenditure.

PROBLEMS

1. From the following, prepare Fire Revenue Account for the year ended 31st March 2004.

Particulars	₹ 000
Claims Paid	2,35,000
Legal Expenses regarding claims	5,000
Premiums received	6,00,000
Reinsurance Premiums	60,000
Commission	1,00,000
Expenses of Management	1,50,000
Provision against unexpired risk on 1.4.2003	2,60,000
Claims unpaid on 1.4.2003	20,000
Claims unpaid on 31.3.2004	35,000
Reserve 50% of the net premium for unexpired risk.	

Sol :

Revenue Account for the year ended 31.3.2004

	Particulars	**Schedule No.**	**Rs. (000)**
I.	Premium earned (Net)	1	5,30,000
	Total – I		5,30,000
II.	Claims Incurred	2	2,55,000
	Commission paid	3	1,00,000
	Operating Expenses	4	1,50,000
	Total - II		5,05,000
III.	Operating Profit = I – II		25,000

Schedules forming part of Financial Statements

Schedule No.1 – Premium earned

	Particulars	**Rs. (000)**	**Rs. (000)**
	Premium received		6,00,000
Less :	Reinsurance premiums		60,000
	Net premium		5,40,000
Less :	i) Unexpired risk provision at the end of the year		
	50% of net premium $\left(5,40,000 \times \frac{50}{100}\right)$	2,70,000	
	ii) Unexpered risk at beginning of the year	2,60,000	10,000
	Total Premium Earned		5,30,000

Schedule No.2 – Claims incurred

	Particulars	Rs. (000)
	Claims paid	2,35,000
Add :	Legal expenses regarding claims	5,000
Add :	Claims unpaid as on 31.3.2004	35,000
		2,75,000
Less :	Claims unpaid as on 1.4.2003	20,000
	Total claims incurred	2,55,000

Schedule No.3 – Commission Expenses

Particulars	Rs. (000)
Commission	1,00,000
Net commission	1,00,000

Schedule No.4 – Operating Expenses

Particulars	Rs.	Rs. (000)
Management expenses		1,50,000
Total		1,50,000

2. On 31st March 2004 the books of Goodluck Insurance Co. Ltd. contained the following particulars in respect of the fire insurance

Particulars	(` 000)	Particulars	(` 000)
Reserve for unexpired risk on 1-4-2003	5,00,000	Expenses of Management (including Rs. 30,000 legal expenses paid in connection with claims)	2,80,000
Additional Reserve on 1-4-2003	1,00,000	Interest and Dividends	65,000
Reinsurance Premiums	75,000	Income tax on above	6,500
Reinsurance recoveries	20,000	Profit on sale of investments	11,000
Premiums	11,20,000	Commission	1,52,000
Estimated liability in respect of outstanding claims:		Claims Paid	6,40,000
On 1-4-2003	65,000		
On 31-3-2004	90,000		

Prepare the Fire Insurance Revenue Account for the year ended 31st March 2004 reserving 50% of the premiums for unexpired risks and keeping an additional reserve of ` 1,00,000.

Sol :

In the books of Good Luck Insurance Co. Ltd.

Revenue A/c for the year ended as on 31.3.2004

	Particulars	Schedule No.	Rs. (000)
I)	Premium earned	1	10,22,500
	Profit on sale of Investment		11,000
	Interest and dividend (Gross)		65,000
	Total - I		10,98,500
II)	Claims Incurred	2	6,75,000
	Commission	3	1,52,000
	Operating expenses	4	2,50,000
	Total - II		10,77,000
III)	Operating Profit = I - II		21,500

Schedules forming part of Financial Statements

Schedule No.1 – Premium earned (Net)

	Particulars	Rs.(000)	Rs.(000)
	Premium received		11,20,000
Less :	Reinsurance premiujms		75,000
	Net premium –		10,45,000
Less :	Unexpired risk as on 31.3.2004 @ 50% net premium	5,22,500	
Add :	Additional Reserve	1,00,000	
		6,22,500	
	Unexpired risk as on 31.4.2003 - (500,000 × 100,000)	6,00,000	22,500
	Total premium earned		10,22,500

Schedule No.2 – Claims incurred

	Particulars	Rs.(000)
	Claims paid	6,40,000
Add :	Legal expenses	30,000
		6,70,000
Less :	Re-insurance recover	20,000
		6,50,000
Add :	Outstanding claims as on 31.3.2004	90,000
		7,40,000
Less :	Outstanding claims as on 1.4.2003	65,000
	Total claims incurred	6,75,000

Schedule No.3 – Commission

Particulars	Rs. (000)
Commission paid	1,52,000
Total	1,52,000

Schedule No.4 – Operating Expenses

Particulars	Rs. (000)
Management expenses	2,80,000
Less : Legal expenses paid for claims	30,000
Total	2,50,000

3. From the following information, prepare a Revenue Account of a Fire Insurance Company for the year ending 31st March 2004.

Particulars	(₹ 000)	Particulars	(₹ 000)
Fire Fund on 31.3.2003	6,00,000	Claims outstanding on 1.4.2003	20,000
Premiums received	4,50,000	Claims outstanding on 31.3.2004	24,000
Premiums due but not received	30,000	Claims recovered under reinsurance	18,000
Premiums paid for reinsurance	10,000	Expenses of Management	84,000
Interest, Dividends and rent (gross)	70,000	Rent Prepaid for Office building	1,000
Income-tax deducted there from	8,000	Loss on sale of office machines	2,000
Profit on sale of investments	7,000		
Sundry Incomes	2,000	Commission to Agents	42,000
Claims paid during the year	3,80,000		
Commission on reinsurance accepted	3,000		

Keep a reserve for unexpired risk equal to 50% of the premiums and additional reserve of ₹ 80,000.

Sol :

Fire Insurance Company

Revenue Account for the year ended as on 31.3.2004

	Particulars	Schedule No.	Rs. (000)
I)	Premium earned	1	7,55,000
	Profit on sale of investments		7,000
	Sundry Incomes		2,000
	Interest, Dividend and Rent (Gross)		70,000
	Total - I		8,34,000

II)	Claims paid	2	3,66,000
	Commission	3	45,000
	Operating expenses	4	86,000
			4,97,000
III)	Operating profit = I - II		3,37,000

Schedules forming part of financial statements

Schedule 1 : Premium earned

Particulars	Rs.(000)	Rs.(000)
Premium received		4,50,000
Add : Outstanding as on 31.3.2004		30,000
		4,80,000
Less : Premium paid for reinsurance		10,000
Net Premium		4,70,000
Add : Unexpired risk on 31.4.2003 –	6,00,000	
Less : Unexpired risk as on 31.3.2004 @ 50%	2,35,000	
Additional Reserve	80,000	2,85,000
Total Premium Earned		7,55,000

Schedule No. 2 – Claims incurred

Particulars	Rs.(000)
Claims paid	3,80,000
Add : Outstanding claims as on 31.3.2004	24,000
	4,04,000
Less : i) Outstanding claims as on 1.4.2003	20,000
ii) Claims recovered under re-insurance	18,000
Total claims incurred	3,66,000

Schedule No.3 – Commmission Expenses

Particulars	Rs.(000)
Commission paid to agents	42,000
Add: Commission on re-insurance accepted	3,000
Total	45,000

Schedule No.4 – Operating expenses

Particulars	Rs.(000)
Management expenses	84,000
Add : Loss on sale of office machines	2,000
Total	86,000

2.10 Reserving Process Followed by Insurance Companies

Q41. Discuss in brief the process of reserving followed by insurance companies.

Ans : **(Imp.)**

Insurance companies need to deal with lot of uncertain scenarios. These firms accept premium from customers and accept liability towards the payment of compensation, in case of any adverse event. These firms sell a variety of insurance policies and are liable to settle a number of claims, against the policies they sell.

Following are the process/methods of reserving followed by insurance companies,

1. Traditional Method

Until the late 1970's insurance companies used to follow the traditional methods of reserving for claims. The practice involved the assessment of all the claims by the insurance company's assessment officer. All the claims made in one single year would be aggregated and an estimate of the reserve requirement for the future year would be prepared.

For example, in the current year, if an insurance company paid claims totalling 470 crores towards claims made by the insured customers then the company would create and set aside a reserve of around 500 crores towards claims for the next financial year.

2. Statistical Estimation Process

Under this process of insurance reserve, a detailed analysis of the policy information is performed. It involves the assessment of each claim which was made previously, the premium amount which is fixed for the customers who desire to avail the specific insurance policy. Statistical models are then employed to arrive at an optimum reserve which would keep the organization liquid as well as profitable.

3. Handlers Judgement

In the case of simple insurance policies, the computation of the reserve amount is based upon the judgement decisions made by experienced company officials who provide an estimated amount of reserve which would be required to cover up for a specific type of claim. For example, claims such as property loss as a result of fire can be easily estimated and settled off.

However in other types of claims such as claims arising as a result of sudden huge natural calamity such as earth quake, floods etc, it is highly complex to arrive at the amount of reserve fund which needs to be maintained by the insurance company to smoothly handle all the claims by the insured customers, who had suffered losses, in such cases, the present day insurance firms are employing complex and powerful computer based statistical software which would provide an optimum amount of reserve that the firm should maintain.

Thus, it may be concluded that there is no one specific procedure of reserving for claims which could be followed by the insurance company. The reserving process and also the method of arriving at such a reserve would vary from one type of insurance policy to another.

Short Question and Answers

1. What do you mean by claim settlement?

Ans :

Claim settlement means paying back the money by the insurance company to the insurance policy holder. A claim is said to be settled when the policy holder duly receives the money which is due to him by the company according to the terms and conditions of policy. The process of claim settlement directly reflects the efficiency and effectiveness of the company. A company which correctly and successfully settles down the claims of clients achieves trustworthiness and loyalty. While the insurance companies which involve litigations in claim settlements owes bad reputation in the market.

Claim settlement of an insurance policy usually takes place in two circumstances,

A) On death of policy holder.

B) On maturity of insurance policy.

2. Define Underwriting.

Ans :

Underwriting can be termed "assumption of liability". It means signing an insurance policy and thereby becoming liable in the face of a specified loss. Underwriting involves the selection of policyholders after thoroughly evaluating all hazards, establishing prices and then determining the terms and conditions of the insurance policy.

The underwriting framework of a company plays a major role in determining the company's standing in the market. The underwriter must aim to generate profits and minimize losses through a well-balanced underwriting policy. One aspect that the underwriter must always bear in mind is that the underwriting must neither be too strict nor too lenient. If the acceptance criteria are very stringent, then the insurer will miss out on several acceptable businesses and may even face losses because of the expenses involved in cancelling business that the marketing person might have initially agreed to. This can be remedied by including enough conditions to make the risk acceptable. On the other hand, if the acceptance criteria are too liberal, the insurance company may face substantial losses and be forced to withdraw from a given line of business.

3. What are the benefits of underwriting?

Ans :

The benefits of underwriting can be summarized as follows :

(i) Product Equitable to Customer

The underwriter should fairly assess the risk in a personal and fix the premium justifiable to the customer.

(ii) Deliverable to the Customer

Consumers are the final authority for buying the products. If the marketers are not able to sell so that the product becomes undeliver-able, the onus is on the underwsriters to carry an introspection of the various factors that caused differences between the consumers and company's expectations.

(iii) Financially Feasible in the Insurance Company

The insurers are not in the business of charity. The underwriting benefit must be reflected by the financial statements. Although, the underwriters are not directly involved in the pricing of insurance products, yet their contribution is an vital as that of actuaries, because they operationalise the business of risk.

4. Define risk sharing

Ans :

Risk sharing means that the premiums and losses of each member of a group of policyholders are allocated within the group based on a predetermined formula. Risk is considered to be shared if there is no policyholder-specific correlation between premiums paid into a captive, for example, and losses paid from the captive's reserve pool. Risk sharing is the practice of distributing risks amongst organizations, departments, teams or individuals.

Sharing risk is often implemented through employer-based benefits that allow for the company to pay a portion of insurance premiums with the employee. Larger companies with more employees can negotiate even lower fees, due to the economies of scale that they bring to the table. In essence, this shares the risk with the company and all employees participating in the insurance benefits. Sharing is a method to drive down costs in order to minimize retention risk. Individuals may find it in their best interest to partake in sharing the risk with matching employer health care and life insurance plans.

This concept is a structural theme behind the state health insurance exchanges mandated by "Obama care." The understanding is that with more participants sharing the risks, the costs of premiums should shrink proportionately. Whether the intended objective is reached is up for debate, as health insurance premiums continue to rise annually. From the health insurance company's perspective, the premiums from healthy members should offset the expenses for the ailing members. In the past, insurance companies could mitigate some of the risk during the enrollment process by limiting or denying coverage to individuals with pre-existing medical conditions.

5. Risk Avoidance

Ans :

Avoidance is the elimination of risk. You can avoid the risk of a loss in the stock market by not buying or shorting stocks; the risk of a venereal disease can be avoided by not having sex, or the risk of divorce, by not marrying; the risk of having car trouble, by not having a car. Many manufacturers avoid legal risk by not manufacturing particular products.

Of course, not all risks can be avoided. Notable in this category is the risk of death. But even where it can be avoided, it is often not desirable. By avoiding risk, you may be avoiding many pleasures of life, or the potential profits that result from taking risks. Those who minimize risks by avoiding activities are usually bored with their life and don't make much money. Virtually any activity involves some risk. Where avoidance is not possible or desirable, loss control is the next best thing.

Ways of Risks Avoidance

There are two ways of avoiding risk. They are as follows,

(a) Risk Transfer

Transferring of risk plays an important role in the financial system. Selling off an asset that act as a source of risk is one of the basic method of transferring risk. Example: Consider a car owner is subjected to two types of risk damage due to accident, reduction in its value or damage due to natural calamities. Therefore, by selling the car he can get rid of all the risks.

(b) Risk Aversion

Risk aversion refers to the technique in which the investor choose one project which is less risker from the other investment projects. If two investment projects have similar cost and expected return is also same, but the return from one of the project is less certain and the return from the other project is more certain, then the project containing high certainty will be selected.

6. Risk Retention

Ans :

Risk retention, (aka active retention, risk assumption), is handling the unavoidable or unavoided risk internally, either because insurance cannot be purchased or it is too expensive for the risk, or because it is much more cost-effective to handle the risk internally. Usually, retained risks occur with greater frequency, but have a lower severity. An insurance deductible is a common example of risk retention to save money, since a deductible is a limited risk that can save money on insurance premiums for larger risks. Businesses actively retain many risks what is commonly called self-insurance because of the cost or unavailability of commercial insurance.

Passive risk retention is retaining risk because the risk is unknown or because the risk taker either does not know the risk or considers it a lesser risk than it actually is.

Types

The following are the different types of retentions,

(a) Planned Retention : Planned retention is the retention under which the risk is recognized. Plans and conscious efforts are made for the assumption of recognized risk. Most organizations prefer planned retention as it is the most convenient technique for risk management. Absence of alternatives also forces the organizations to adapt planned retention.

(b) Unplanned Retention: Unplanned retention refers to the retention made by a firm without the recognition of exact risk. If the organization under estimates the possible loss associated with the risk, an unplanned retention type is believed to be adopted by the organization.

(c) Unfunded Retention : Unfunded retention refers to the retention where no funds are arranged in advance for the payment of losses.

(d) Funded Retention : When the organization makes an arrangement of funds in advance to pay for the losses that may occur in the future, it is said to follow a funded retention type. Funded retention may be in any of the following type,

(i) Credit : A credit line may be drawn up by the manager to fund the losses that arise as a result of retained risks. There is no proper source for payment of huge losses unless the credit line is decided by the manager.

(ii) Reserve Funds : A firm may establish a reserve fund to pay off losses arising from the risks retained by the firm. In case of huge losses, reserve funds may prove to be ineffective.

(iii) Self-Insurance : A self-insurance may also be used to fund the risk of the firm. This is possible when firm has large units that have the ability to predict losses. An organization can refund the expected losses by introducing special funds for the required purpose. Self-insurance does not involve transfer of risk.

(iv) Captive Insurers : Under this method, organizations bring together risk retention and risk transfer. The risk is retained by the firm and the payment for losses is made by the insurers.

7. Risk management.

Ans :

Risk management is the branch of the discipline '*management*' which is concerned with the overall management of risk and concerning aspects. More specifically, risk management is the study of identifying, analyzing, interpreting, and controlling of different economic risks which can endanger the individual or business organization.

''Define risk management as: The identification, analysis and economic control of those risks that can threaten the assets or earning capability of an enterprise.''

''Risk management is the systematic and efficient handling or pure risks.''

From the mentioned definitions above, it will be noted that these definitions emphasizes human effort and the organizational structure. Risk management similarly utilizes men, materials and machines in accomplishing its objectives, and furthermore, the application of risk management tools and the implementation of decisions in this area require highly trained personnel and proper equipment.

8. Define claim.

Ans :

As insurance claim is a formal request to an insurance company for coverage or compensation for a covered loss or policy event. The insurance company validates the claim and, once approved, issue payment to the insured or an approved interested party on behalf of the insured.

Insurance claims cover everything from death benefits on life insurance policies to routine and comprehensive medical exams. In many cases, third-parties file claims on behalf of the insured person, but usually only the person(s) listed on the policy is entitled to claim payments.

A paid insurance claim serves to indemnify a policysholder against financial loss. An individual or group pays previous as consideration for completion of an insurance contract between the insured party and an insurance carrier. The most common insurance claims involve costs for medical goods and services, physical damage and liability resulting from the operation of automobiles, property damage and liability for dwellings (homeowners, landlords, and renters), and the loss of life.

9. Reserves

Ans :

According to the American Institute of Accounting, "the use of the term reserve by limited to indicate, that an undivided part of the asset is being held or retained for general or specific reserve". This in simple terms, reserve can be defined as "A part of the profit which is kept aside by the firm to meet up any future contingency, liability or make adjustment for the decrease in the value of an asset".

10. Insurance Reserves

Ans :

Insurance reserve refers to the monetary reserve which is set aside by insurance companies to pay for claims by their customers. This, is known as insurance reserve. Thus, in simple words, it refers to the financial reserves which are maintained by every type of insurance organization.

11. Define Insurance Accounting.

Ans :

The accounting process followed by insurance companies for maintaining their accounts of clients and claims is referred as insurance accounting. General insurance companies maintains accounting books as per the guidelines given by Insurance Regulatory and Development Authority (IRDA).

Choose the Correct Answer

1. "A contract that pledges payment of an agreed upon amount to the person (or his/her nominee) on the happening of an event covered against" is technically known as [b]

   (a) Death coverage (b) Life insurance

   (c) Savings for future (d) Provident fund

2. Which of the following is the regulator of insurance sector in India? [c]

   (a) RBI (b) AMFI

   (c) IRDA (d) SEBI

3. The insurance companies collect a fixed amount from its customers at a fixed interval of time. What is it called? [c]

   (a) Instalment (b) Contribution

   (c) Premium (d) EMI

4. The Caregiver Insurance Company chose to write insurance for risk in many different locations. It found that this was an effective way to balance premiums with losses and expenses. Selecting risk in this manner is called [b]

   (a) diversity of type of risk. (b) diversity of location.

   (c) volume. (d) risk concentration.

5. Full Coverage Insurance Ltd. issues policies on behalf of other insurance companies and charges them a fee for the use of its name. This arrangement is an example of, [b]

   (a) unearned premium reserves.

   (b) fronting.

   (c) a reciprocal insurance exchange.

   (d) insurance pools.

6. Different types of life insurance claims are [d]

   (a) Death claim (b) Maturity claim

   (c) Survival Benefit (d) All the above

7. There are steps involved in death claim procedure. [c]

   (a) 6 (b) 7

   (c) 5 (d) 4

8. Unnatural causes of death includes. [c]

   (a) Suicide (b) Accident

   (c) Both (a) and (b) (d) Old age

9. Underwriting helps in risk pooling and [a]
   (a) Fair Pricing (b) Waiver of Premium
   (c) Guaranteed Purchase Option (d) Accelerated Benefit's Rider

10. FUP stands for [d]
   (a) Fixed Unpaid Premium (b) Full Unpaid Premium
   (e) Final Unpaid Premium (d) First Unpaid Premium

11. Benefits paid comes under schedule ________ . [a]
   (a) Schedule - 4 (b) Schedule - 3
   (c) Schedule - 2 (d) Schedule -1

12. The profit or deficiency is determined by preparing a statement called [c]
   (a) Profit and Loss A/c (b) Trading A/c
   (c) Valuation Balance Sheet (d) Balance Sheet

13. In the _____ account, claims must be taken after deducting the re-insurance claim. [b]
   (a) Net Revenue A/c (b) Revenue A/c
   (c) Profit and Loss A/c (d) Balance Sheet

14. Reinsurance premium is given by reinsurer to the [d]
   (a) Insurer (b) Insured
   (c) Reinsured (d) Reinsurer

15. In memorandum trading account the sales is shown on [b]
   (a) Debit side (b) Credit side
   (c) Both (a) and (b) (d) None of the above

16. Risk class where the anticipated risk is higher than the average risk [c]
   (a) Preferred class (b) Standard class
   (c) Sub standard class (d) None of these

17. Risk class where the inherent risk is lesser than average risk then such risk class is called [a]
   (a) Preferred class (b) Standard class
   (c) Sub standard class (d) None of these

18. IIRM is an international education and research organization which was setup jointly by IRDA of India and [c]
   (a) Central government (b) Supreme court
   (c) State Government (AP) (d) State Government (TN)

19. From the following, which is not a risk sharing method [d]

    (a) Avoidance (b) Loss control

    (c) Retention (d) Remission

20. Expand the term IFRS [c]

    (a) Indian Financial Reporting Standards

    (b) Indian Financial Reporting Systems

    (c) International Financial Reporting Standards

    (d) International Financial Reporting Systems

Fill in the Blanks

1. First step in death claim settlement ________.
2. IRDA stand for ________.
3. ________ refers to the demand made by an insured or beneficiary to the insurer to make payment of insurance policy benefits.
4. ________ refers to the practice of a government collecting money from its citizens to pay for public services.
5. Taxation on Annuity or Pension plans is discussed under ________.
6. If an insured dies before expiry of term of policy then it results in ________.
7. If a person is not heard for 7 years and found missing then court issue decree of ________.
8. Under IRDA regulations, insurer must take decision within ________ of receiving claim papers whether to accept or reject a death claim.
9. Surrender value is shown in Schedule - 4 as an ________.
10. ________ is the premium concerning the general insurance business which is received in advance by insurance company.
11. There are ________ schedules which form the part of financial statements in general insurance company.
12. IIRM stands for ________ .
13. RMAC stands for ________ .
14. ORMC stands for ________ .
15. IBNR stands for ________ .
16. ________ is the money that is earmarked for the eventual claim payment.

Answers

1. Information of death
2. Insurance Regulatory and Development Authority
3. Claim
4. Taxation
5. Section 80CCC
6. Death Claims
7. Presumption of Death
8. 30 days
9. Expenditure
10. Reserve for unexpired risk
11. 15
12. The Institute of Insurance and
13. Risk management advisory Committee
14. Operational Risk Management Committee
15. Incurred but not reported
16. Claims reserve

FACULTIES OF COMMERCE

B.Com. IV – Semester (CBCS) Regular Examination

Model Paper - I

PRACTICE OF LIFE AND GENERAL INSURANCE

(Common Paper for General / Computers / Computer Applications / Advertising / Foreign Trade / and Tax Procedure Courses)

Time : $1^1/_2$ Hours] **[Max. Marks : 40**

PART - A (2 × 5 = 10 Marks)

[Short Answer Type]

Note: Answer any two of the following questions not exceeding one page each.

ANSWERS

1. What are the features of IRDA ? **(Unit-I, SQA-14)**
2. Define Rebate. State the various modes of Rebates. **(Unit-I, SQA-3)**
3. Risk management. **(Unit-II, SQA-7)**
4. What do you mean by claim settlement? **(Unit-II, SQA-1)**

PART - B (2 × 15 = 30 Marks)

[Essay Answer Type]

Note: Answer all the questions in not exceeding 4 pages each.

5. (a) What are the principles of Life Insurance? **(Unit - I, Q.No. 4)**

OR

(a) What are the differences between Life Insurance and General Insurance? **(Unit - I, Q.No. 18)**

6. (a) What do you mean by claim settlement? Explain the procedure for claim settlement for life insurance policies. **(Unit - II, Q.No. 2)**

OR

(a) Define Insurance Accounting. State the recent developments of insurance accounting. **(Unit - II, Q.No. 38)**

FACULTIES OF COMMERCE

B.Com. IV – Semester (CBCS) Regular Examination

Model Paper - II

PRACTICE OF LIFE AND GENERAL INSURANCE

(Common Paper for General / Computers / Computer Applications / Advertising / Foreign Trade / and Tax Procedure Courses)

Time : $1^1/_2$ Hours] [Max. Marks : 40

PART - A (2 × 5 = 10 Marks)

[Short Answer Type]

Note: Answer any two of the following questions not exceeding one page each.

ANSWERS

1. What is loading and premium loading? **(Unit-I, SQA-4)**
2. What is Surrender Value? **(Unit-I, SQA-6)**
3. Define Underwriting. **(Unit-II, SQA-2)**
4. Define claim. **(Unit-II, SQA-8)**

PART - B (2 × 15 = 30 Marks)

[Essay Answer Type]

Note: Answer all the questions in not exceeding 4 pages each.

5. (a) Discuss the calculation of premium for different types of policies. **(Unit - I, Q.No. 8)**

OR

(a) Explain about IRDA and reserve for unexpired risk along with its treatment. **(Unit - I, Q.No. 44)**

6. (a) "Age, Gender, Family, and other affect insurability" - Elucidate. **(Unit - II, Q.No. 9)**

OR

(a) Explain the implication of income tax of life insurance companies. **(Unit - II, Q.No. 18)**

FACULTIES OF COMMERCE

B.Com. IV – Semester (CBCS) Regular Examination

Model Paper - III

PRACTICE OF LIFE AND GENERAL INSURANCE

(Common Paper for General / Computers / Computer Applications / Advertising / Foreign Trade / and Tax Procedure Courses)

Time : 1$^1/_2$ Hours] **[Max. Marks : 40**

PART - A (2 × 5 = 10 Marks)

[Short Answer Type]

Note: Answer any two of the following questions not exceeding one page each.

ANSWERS

1. Cover Note **(Unit-I, SQA-7)**
2. What is Fire Insurance ? **(Unit-I, SQA-9)**
3. Risk Retention **(Unit-II, SQA-6)**
4. What are the benefits of underwriting? **(Unit-II, SQA-3)**

PART - B (2 × 15 = 30 Marks)

[Essay Answer Type]

Note: Answer all the questions in not exceeding 4 pages each.

5. (a) Explain briefly about Soft and Hard Markets in general insurance. **(Unit - I, Q.No. 47)**

OR

(a) Explain the different types of General Insurance Products. **(Unit - I, Q.No. 20)**

6. (a) What is financial planning? Explain the role of life insurance policies in financial planning. **(Unit - II, Q.No. 12)**

OR

(a) What are the steps involved in risk management process? **(Unit - II, Q.No. 26)**